

**Port Commission
City and County of San Francisco
Port of San Francisco**

Independent Auditor's Report,
Management's Discussion and Analysis, and
Financial Statements

For the Years Ended
June 30, 2019 and 2018



Certified
Public
Accountants

**PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
PORT OF SAN FRANCISCO**

For the Years Ended June 30, 2019 and 2018

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Independent Auditor's Report

The Port Commission, the Honorable Mayor, and
the Board of Supervisors of the City and County
of San Francisco, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Port Commission, City and County of San Francisco (City), Port of San Francisco (Port), an enterprise fund of the City, as of and for the years ended June 30, 2019 and 2018, and the related notes to the financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Port as of June 30, 2019 and 2018, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 1 to the financial statements, the financial statements present only the Port enterprise fund and do not purport to, and do not, present fairly the financial position of the City as of June 30, 2019 and 2018, the changes in its financial position, or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis identified in the accompanying table of contents be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 4, 2019, on our consideration of the Port's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Port's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Port's internal control over financial reporting and compliance.



San Francisco, California
December 4, 2019

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Management's Discussion and Analysis (Unaudited)
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Introduction

This discussion and analysis is a narrative overview and analysis of the financial activities of the Port of San Francisco (Port). It serves as an introduction to the audited financial statements, which can be found on pages 20 to 25 of this report. This overview should be read in conjunction with the more detailed information contained within the accompanying financial statements.

The Port is a self-supporting enterprise department of the City and County of San Francisco (City), and its financial statements are included in the City's basic financial statements. Only the accounts of the Port are included in the financial statements that follow. The Port Commission is responsible for seven and one-half miles of waterfront property, which was transferred in trust from the State of California to the City in 1969. The Port's revenue is derived primarily from property rentals to commercial and industrial enterprises and from maritime operations, which include cargo, ship repair, fishing, harbor services, cruise and other maritime activities. Additional information concerning the Port's organization and the basis of presentation for this financial report is contained in Note 1 and Note 2 to the financial statements (pages 26 to 31).

Financial Statement Overview

The statements of net position present information on all of the Port's assets, deferred outflows of resources, liabilities, and deferred inflows of resources with the sum of these elements reported as "net position." Increases and decreases in net position serve as a useful indicator of the changes in financial position of business enterprise entities like the Port.

The statements of revenues, expenses and changes in net position present information that shows how the Port's net position changed during the most recent two years. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. This statement also reports revenues and expenses for some items that will result in cash flows in future fiscal periods (e.g. uncollected rents from tenants and earned and unused vacation leave).

The statements of cash flows present information about the cash receipts and cash payments of the Port during the most recent two fiscal years. This statement shows the changes in cash and cash equivalents as a result of operating, investing, capital, and financing transactions. When used with related disclosures and information in the other financial statements, the information in the statements of cash flows helps readers assess the Port's ability to generate net cash flows, its ability to meet its obligations as they come due, and its need for external funding.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes follow the financial statements and can be found on pages 26 to 68 of this report.

The following is a presentation of condensed financial information derived from the financial statements.

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Condensed Financial Information – Port of San Francisco

Comparative Net Position (in thousands)

	June 30,			2019-2018 Change	2018-2017 Change
	2019	2018	2017		
Current and other assets	\$ 227,819	\$ 214,424	\$ 208,502	\$ 13,395	\$ 5,922
Capital assets	464,272	434,702	427,742	29,570	6,960
Total assets	<u>692,091</u>	<u>649,126</u>	<u>636,244</u>	<u>42,965</u>	<u>12,882</u>
Deferred outflows of resources	14,547	14,672	20,916	(125)	(6,244)
Current liabilities	31,925	32,221	26,505	(296)	5,716
Noncurrent liabilities	234,166	226,424	238,705	7,742	(12,281)
Total liabilities	<u>266,091</u>	<u>258,645</u>	<u>265,210</u>	<u>7,446</u>	<u>(6,565)</u>
Deferred inflows of resources	9,909	3,201	2,210	6,708	991
Net position:					
Net investment in capital assets	334,188	305,609	298,928	28,579	6,681
Restricted	14,467	20,738	24,365	(6,271)	(3,627)
Unrestricted	81,983	75,605	66,447	6,378	9,158
Total net position	<u>\$ 430,638</u>	<u>\$ 401,952</u>	<u>\$ 389,740</u>	<u>\$ 28,686</u>	<u>\$ 12,212</u>

Changes in Net Position (in thousands)

	Year Ended June 30,			2019-2018 Change	2018-2017 Change
	2019	2018	2017		
Revenues:					
Operating revenues	\$ 122,033	\$ 109,769	\$ 113,353	\$ 12,264	\$ (3,584)
Nonoperating revenues	27,860	6,463	5,288	21,397	1,175
Capital contributions	1,909	2,626	1,822	(717)	804
Total revenues	<u>151,802</u>	<u>118,858</u>	<u>120,463</u>	<u>32,944</u>	<u>(1,605)</u>
Expenses:					
Operating expenses	112,108	96,804	114,075	15,304	(17,271)
Nonoperating expenses	11,008	5,844	4,318	5,164	1,526
Total expenses	<u>123,116</u>	<u>102,648</u>	<u>118,393</u>	<u>20,468</u>	<u>(15,745)</u>
Change in net position	28,686	16,210	2,070	12,476	14,140
Net position, beginning of year, as restated	<u>401,952</u>	<u>385,742</u>	<u>387,670</u>	<u>16,210</u>	<u>(1,928)</u>
Net position, end of the year	<u>\$ 430,638</u>	<u>\$ 401,952</u>	<u>\$ 389,740</u>	<u>\$ 28,686</u>	<u>\$ 12,212</u>

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Financial Analysis

Total net position at June 30, 2019 of \$430,638,000 was \$28,686,000 higher than the net position at June 30, 2018. Comparatively, in 2018 net position increased \$12,212,000 and in 2017 net position increased \$2,070,000. The largest portion of the Port's net position is represented by the net investment in capital assets: 78% on June 30, 2019, 76% on June 30, 2018, and 77% on June 30, 2017. This component of net position consists of capital assets net of accumulated depreciation/amortization and reduced by the outstanding balances of debt attributable to the acquisition, construction, and improvement of those assets. The total net investment in capital assets (\$334,188,000 on June 30, 2019) does not represent funds accessible for future spending. The resources needed to pay outstanding debt used to acquire capital assets must be provided from other sources (i.e. other Port assets or operating revenues). The remaining portion of net position on June 30, 2019 consists of \$14,467,000 restricted for specific capital project expenditures and \$81,983,000 that is unrestricted and available to meet future capital requirements and ongoing obligations. Capitalized project expenditures have fluctuated in recent years. There was a net increase to capital assets in 2019 of \$29,570,000, which compares to a net increase to capital assets of \$6,960,000 in 2018, and a net decrease of \$3,108,000 in 2017. The funding for the acquisition and construction of capital assets (largely facility improvements) is reflected in the sources and uses of working capital and changes to liabilities and other obligations. Grants and other capital contributions also fund certain capital projects.

In 2019, a few nonrecurring events affected the increase in net position and largely explains the \$28,686,000 increase in net position. First, on May 1, 2019, the Port received the South Beach Harbor (SBH) operations from the Office of Community Investment and Infrastructure (OCII), successor agency to the redevelopment agency, along with the related assets and liabilities (Note 13). In 2012, the Board of Supervisors adopted Resolution No. 11-12 to provide for the transition of redevelopment agency assets and functions pursuant to Assembly Bill 26 (AB26), which by operation of law dissolved redevelopment agencies in the State of California. The Port and the OCII negotiated a memorandum of agreement covering the termination of Port agreements and providing for the transfer of certain assets and operations of the Rincon Point South Beach Project to the Port. Assembly Bill No. 1484 significantly amended AB26 and delayed the transition plans initiated by the City. In 2019, the Port received the SBH operations, which added \$18,340,000 to the Port's net position. Second, the Port made a \$6,500,000 contribution to the Pier 70 development area as an investment to fund early-stage development costs, decreasing its net position. Finally, the sale and transfer of the Ferry Building master lease generated \$10,300,000 of nonrecurring income increasing net position.

The net increase in current assets of \$13,395,000 and increase in noncurrent liabilities of \$7,742,000 in 2019 is principally due to a \$14,958,000 receivable from the Mayor's Office of Housing and Community Development (MOHCD) and related \$14,501,000 unearned revenue related an affordability housing project agreement at Seawall Lot 322-1 ("88 Broadway") entered in September 2018. 88 Broadway is subject to the Burton Act and the public trust doctrine. However, provisions under Senate Bill 815 authorized the Port to lease certain seawall lots for non-trust purposes, including housing, for a period up to 75 years at fair market value. This affordable housing project will provide homes for low-income families and seniors. In March 2019, the Port entered into a ground lease, which conveyed property rights under which, the project site is leased to the developer, for an initial term of 75 years. The Port will recognize revenue from the agreement over the lease period of 75 years. While the increase in current assets is largely explained by the \$14,958,000 receivable, the \$7,742,000 increase in noncurrent liabilities is primarily due to the \$14,501,000 increase in unearned revenue, offset by a decrease of \$5,703,000 in net pension liability, and further offset by a decrease in net OPEB (e.g. Retiree Health Benefits) liability by \$1,794,000. The decrease in net pension liability is largely due to greater investment returns than projected. The decrease in Net OPEB

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liability is due to a change in plan experience differing from that anticipated by economic or demographic assumptions. The remaining difference in noncurrent liabilities is due to changes in several accounts related to additional pollution remediation liability (Note 17), Cal Boating Loans assumed with the receipt of SBH (Note 8), and amortization of tenant rent credits. The net decrease in noncurrent liabilities of \$12,281,000 in 2018 reflects decreases in the net pension liability, estimated pollution remediation obligation, and scheduled long-term debt payments, offset by an increase in net OPEB liability. The year over year fluctuations in current liabilities as of June 30, 2019, and 2018 are reflective of volume of in-progress capital project work, related accrued obligations, and the current portion of the assumed Cal Boating loans.

Operating revenues in 2019 and 2018 supported current year operation and maintenance expenses before depreciation and amortization. Nonoperating revenues include investment income, operating grants, and the special item. Capital contribution revenues fluctuate with the level of capital grant revenues realized from grant-funded construction activities. Historically, capital contribution revenues have also included City direct contributions for certain projects and general obligation bond proceeds allocated to fund the Port's open space and park improvement projects. Nonoperating expenses are costs outside of normal operations and are reported in the nonoperating revenues and expenses section. Examples include any costs for pier removal, demolition work and other asset disposition costs and any associated gains and losses from those capital events. Information concerning significant variances and nonrecurring items are included in the more detailed discussion that follows.

The statements of revenues, expenses and changes in net position on page 23 present the Port's operating revenues in more detail by industry revenue types. Operating revenues for the year ended June 30, 2019 increased by \$12,264,000 or 11.2%. This increase is principally due to a nonrecurring participation income of \$10,300,000 from the sale and transfer of the Ferry Building master lease. The remaining increase is explained by a \$2,698,000 increase in commercial and industrial rent, reflecting strength in local economy, offset by relatively small fluctuations in remaining operating lines of revenue. Comparatively, in 2018, operating revenues decreased by \$3,584,000 or 3.2% primary due to the loss of one-time other operating revenues from the sale of The Piers in 2017.

The Port continues to benefit from a good volume of cruise calls and the higher fees and charges assessed since the James R. Herman Cruise Terminal at Pier 27 opened in September 2014. Cruise revenues of \$7,947,000 for 2019 were \$46,000 higher than 2018 revenues. Comparatively, 2018 was greater than 2017 by \$495,000. There were 83, 78, and 77 passenger cruise calls in 2019, 2018 and 2017, respectively. Also, the cruise passenger counts were 280,000, 275,000, and 272,000 in 2019, 2018 and 2017, respectively. Princess Cruises continues a year-round schedule with several vessels sailing from San Francisco. Participation income is received by the Port for special events, parking, and other activities occurring at this facility.

Cargo revenues decreased by \$842,000 between 2019 and 2018, primarily due to a \$792,000 decline in storage revenues, due to the conclusion of a nonrecurring arrangement to store vehicles at Pier 80. Excluding this loss of one-time revenues in 2019, recurring cargo revenues appear stable. The ship repair industry in the San Francisco Bay Area, has become increasingly competitive and in May 2017 the operator of the Pier 70 shipyard abandoned its leasehold. The Port has since issued two unsuccessful Requests for Proposals for a new shipyard operator and continues to explore options for the Pier 70 shipyard. Fishing revenues increased \$89,000 or 4% in 2019, primarily due to a general berthing rate increase and a salmon fishing season that was not shortened. Fishing revenue in 2018 decreased mostly due to a limited salmon season lasting only 19 days. The other maritime revenue decreased by \$93,000 in 2019 primarily due to

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one-time revenue in 2018 as the Port drew on a letter of credit related to a shipyard operator abandoning the leasehold.

Other operating revenues include construction and event permit fees, other one-time transaction fees, and expense recoveries realized or realizable from significant development projects. These revenues fluctuate from year to year since they are largely derived from construction activities on Port property and the timing of specific project transactions. In 2019, other operating revenues increased by \$10,029,000 due primarily to the \$10,300,000 received from the sale and transfer of the Ferry Building Master lease. In 2018, there was a \$9,040,000 decrease in other operating revenues as there were significant one-time revenues in 2017, from the sale and transfer of The Piers project and one-time revenues from the settlement involving the former shipyard operator.

Capital grants and other contributions usually consist of funds from federal, state, and local grant agencies, which provide funding for several of the Port's capital projects. This revenue source fluctuates based on available grant funds and the capital work actually in progress at the Port. Overall, capital grants and contributions declined \$717,000, due to a decline in grant revenue from the Goods Movement Locomotive project, which recognized revenue primarily in 2018.

Total expenses of \$123,116,000 (condensed summary on page 4) for 2019 represent a \$20,468,000 increase from 2018. Comparatively, 2018 was lower than 2017 by \$15,745,000. The statements of revenues, expenses and changes in net position on page 23 present the Port's operating and nonoperating expenses in greater detail. Information concerning operating significant variances and nonrecurring items is presented in the more detailed discussion that follows. Operating expense changes in 2019 and 2018 are highlighted below:

	Increase / (Decrease)	
	2019	2018
Personal services	\$ (3,025,000)	\$ (7,068,000)
Contractual services	1,091,000	6,378,000
Utilities	102,000	26,000
Materials and supplies	352,000	(852,000)
Depreciation and amortization	6,830,000	(6,413,000)
General and administrative	262,000	(760,000)
Services provided by other City departments	(592,000)	301,000
Pollution remediation	9,316,000	(8,453,000)
Other	968,000	(430,000)

Despite increases in salary and mandatory fringe benefit costs, pursuant to collective bargaining agreements, the decrease in personal services is primarily due to a net decrease of \$2,540,000 in pension and OPEB expense. In 2019, pension expense decreased by \$1,363,000 and OPEB expense decreased by \$1,177,000. The decreased pension expense is primarily due to impact of actual investment returns outperforming projected investment returns. Comparatively, in 2018, pension expense decreased by \$9,384,000 and OPEB expense decreased by \$790,000. The 2018 decrease in pension expense was due to actual investment returns outperforming projected and although GASB 75 – Other Postemployment Benefits was implemented in 2018, the year over year impact on personal services was not significant. The financial statements for 2019 and 2018 now reflect both Pension and OPEB liabilities using similar actuarial and accounting standards to measure expenses and the related retirement liabilities. More detailed

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information concerning pension and OPEB are in Note 10 beginning on page 45 and Note 12 beginning on page 52, respectively.

The level of contractual services recorded as operating expense fluctuates with the volume of project-related activities and the work phase of these projects. Preliminary conceptual design work, feasibility analyses, environmental investigations, hazardous material removal and demolition costs are typically expensed when incurred. The Real Estate and Development Division has been actively working on several major development projects that are in various stages of negotiation, entitlement process or early implementation. Significant planning work is also in progress with both the Embarcadero Seawall Program (Seawall Program) and the Mission Bay Ferry Landing project. Contractual services increased \$1,091,000 or 6% primarily due to an increase in spending for the Crane Cove Park, Mission Bay Ferry Terminal, and Pier 31.5 Alcatraz Ferry Embarkation projects.

Utility cost increased by \$102,000, which is primarily due to an overall increase in electricity costs of \$144,800 offset by a \$42,000 decrease in water and sewer costs. The electrical costs include shoreside power usage costs, which are pass-through costs and recovered in cruise revenues. Materials and supplies fluctuate with the type and volume of maintenance and repair work that the Port performs during the fiscal year. In 2019, the Port had slight increases in computer supplies, small tools, and maintenance supplies. The increase in depreciation and amortization expense in 2019 is due to a one-time downward adjustment in fiscal year 2018, when the City implemented a new enterprise financial system. The increase in general and administrative expense is principally due to a higher overhead costs from the City and higher spending for rents.

Total service reimbursements to other City departments were \$18,718,000 in 2019, a net decrease of \$592,000 from 2018 or 3% decrease. This represents interdepartmental work orders between the Port and other City departments and reflects a little change year over year. This follows an increase of \$301,000 in 2018 from 2017.

In 2019, pollution remediation expense involving capping contaminated soil was \$1,105,000. This remediation expense was caused by a change in the scope of a project located in the Pier 70 development area. However, in 2018, pollution remediation was a negative expense of (\$8,211,000), resulting in a \$9,316,000 year over year increase. In 2018, the Port entered into a disposition and development agreement with a developer for 28-acre Waterfront site at Pier 70. The developer assumed substantial responsibility for capping contaminated soil in the Pier 70 project area in accordance with the Risk Management Plan (RMP) for the premises. As such, the Port reduced the related pollution remediation obligation by \$8,211,000 in 2018 (see Note 17). The variances in other expenses reflect the change in estimate related to general liability claim costs and expenses, volume of small equipment purchases and the level of transaction activities that require permits, licenses and sales tax.

The 2019 increase in other expenses of \$968,000 is primarily due to a \$663,000 reduction in judgment and claims expense in 2018, as the Port's general legal liability decreased because certain claims were resolved. As there was no change in the Port's general legal liability in 2019, other expenses increased by this amount. The remaining increase in 2019 other expenses is attributed to various costs such as sales and use tax, credit card processing, and license and filing fees. In 2018, the decrease in other expenses was primarily due to reducing the general legal liability and recording a negative \$663,000 judgment and claims expense.

Nonoperating revenues and expenses, other than interest income and expense, tend to fluctuate widely based on largely nonrecurring transaction activities or events. Investments are reported at fair value and

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the corresponding change in fair value is reported along with interest and investment income. Operating grants consist of financial assistance received from various agencies for noncapital purposes, such as special studies, disaster response training, and environmental investigations. Nonoperating revenues increased \$21,397,000 in 2019 and nonoperating expense increased \$5,164,000. The Port's receipt of the SBH operations from the OCII increased nonoperating revenues by \$18,340,000. This transaction is recorded as a special item on statement of revenues, expenses and net position. Also, the \$3,958,000 increase in interest and investment income was primarily due to unrealized gains and interest earnings from the Treasury Pool. The increase in nonoperating expenses was primarily due to the Port's \$6,500,000 contribution to the Pier 70 development project, to pay for entitlement and other early development costs (Note 6). The Port expects to recover this contribution through future special taxes and/or future tax increment with interest.

Capital Asset and Debt Administration

Capital Assets

The Port's capital assets as of June 30, 2019 and 2018, respectively, were \$464,272,000 and \$434,702,000, net of accumulated depreciation/amortization. Principal capital assets include land, certain street and road improvements, pier promenades, pier substructure, buildings and related improvements, vehicles, equipment and furniture. More information concerning the Port's capital assets can be found in Note 6 on pages 35-36 of this report.

Significant project appropriations cover capital projects planned and in-progress, including the pending expenditure of the debt issuances discussed below and the general obligation bond proceeds allocated to open space and park projects along the waterfront. As of June 30, 2019, the budget file indicates over \$116,371,000 in appropriations for Port capital projects. The Port had firm purchase and contract commitments at June 30, 2019 of approximately \$21,234,000 for various capital projects.

Major capital asset related events of 2019 included the following:

- ***Crane Cove Park*** - Crane Cove Park, one of the Port's Blue Greenway projects, will be a major new open space in the Union Iron Works National Historic District located at Pier 70. This site was part of an operating shipyard for more than 100 years and is being transformed into public open space, using multiple construction contracts. In November 2018, the Port awarded a contract to complete the majority of park construction and improvements. The Port has made progress on the project with beach in-water work commencing in June 2019. Project completion is anticipated in 2020. See the development activities section below for more information.
- ***Pier 31.5 (Alcatraz Ferry Embarkation) Substructure Repair*** - Pier 31.5 is the site of the National Park Service's Alcatraz Ferry operations. This project included repairs to the Pier 31.5 marginal wharf and infill wharf and adjacent apron substructures; repairs to portions of the Pier 33 substructure and apron; repairs to a portion of the Pier 31 shed substructure; and installation of sleeves on some concrete apron piles at Pier 31. The repair also included upgrading the entire driveway along the Pier 31.5 marginal wharf to accommodate heavy loads.
- ***Pier 94 Backlands Improvements Project*** - The Pier 94 Backlands is an approximately 47-acre expanse of formerly largely undeveloped land in the Port's southern waterfront area bounded by Amador Street and Cargo Way. This project made improvements to approximately 23 acres of the site to create approximately 16 acres of leasable land parcels. The improvements included creation of a storm water management system, landscaping, capping of a regulated landfill area, installation of lighting and other utilities, and the construction of a new access road.

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- ***Pier 68 Shipyard Power Relocation*** - The Shipyard Power Relocation and High Voltage Redistribution Project replaced aged electrical infrastructure throughout the Pier 68 Shipyard. This project removed, replaced and properly disposed of all PCB oil-containing transformers and electrical equipment located at the shipyard, and installed new switch gear and power routing equipment that will allow for more efficient and effective power consumption and use at the facility.
- ***Pier 27 Passenger Shelter*** - This project installed a steel-framed passenger shelter, approximately 2,600 square feet, at the ground transportation area of the Pier 27 Cruise Terminal. The new passenger shelter replaced the temporary non-permitted shelter and provides weather protection for cruise passengers transferring to and from the cruise terminal by bus or automobile.
- ***Pier 23 MEP Upgrade*** - The Pier 23 Mechanical Electrical Plumbing (MEP) upgrade project improved the lighting, water and sewer systems at Pier 23. Work scope included the replacement of the existing water service with a 4-inch water service, running the length of the shed, with new backflow preventer. The project also installed an above deck 8-inch sanitary sewer riser which will allow future above deck sewer connections. Additionally, the project replaced existing shed lighting with new energy efficient LED fixtures and installed emergency egress lighting for safety.
- ***Pier 45 Public Restroom Improvement*** - This project constructed a new men's and women's public restroom building inside Pier 45 Shed A. The new public restrooms consist of a 400 square foot structure adjacent to two existing single-user restrooms constructed in 1993. These restrooms will provide much-needed public restroom facilities at Fisherman's Wharf.

Other significant construction in progress at June 30, 2019 includes Pier 35 maintenance dredging and improvements to the Pier 29 substructure. The Port's maintenance dredging program is needed to maintain depths for vessels in support of maritime commerce and includes required testing of dredge sediments for contaminants. In FY 2019, the Port performed dredging at Pier 35. The Pier 29 substructure project repaired approximately 17,000 square feet of the pier including underdeck improvement and overwater repairs to soffits, beams, and piles. This project strengthened the Pier 29 substructure and created future leasable area.

Debt Administration

Detailed information concerning the Port's long-term obligations can be found in Note 8 on pages 37-43 of this report. As of June 30, 2019, the Port had long-term debt obligations of \$88,132,000 including \$3,079,000 that is due during the next fiscal year. Total debt outstanding consists of \$50,145,000 in revenue bonds, \$30,010,000 in certificates of participation, and \$7,977,000 in a loan that is secured by specified revenue sources.

The Port did not issue new debt in 2019 and 2018. The 2014 revenue bonds were issued with long-term credit ratings of "A1", "A-" and "A" from Moody's Investors Services, Standard & Poor's Ratings Services (S&P) and Fitch Ratings, respectively. In 2019, Fitch Ratings affirmed the Port's "A" bond credit rating. In 2018, S&P and Fitch Ratings affirmed the Port's "A" bond credit rating.

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Economic and Other Factors

Economy

The Port takes general economic conditions into consideration when preparing budgets and forecasts. Uncertainties in the domestic and global economies have an impact on the Port and its tenants and customers. The Port's overall rental revenue stream remains stable and has seen some growth in recent years. Revenue losses to the Port during economic downturns typically appear as rent payment delinquencies, larger write-offs of uncollectible accounts, and some fluctuation in overage rents (percentage rent obligation based on tenant-reported sales, usually in excess of an agreed minimum). Note 9 (pages 44-45) contains required financial statement disclosure information covering the future rental income stream from minimum rents over the noncancelable term of active operating leases.

San Francisco's economy continues to exhibit strength and Port revenues generally continue to reflect a degree of strength and stability. Cautious optimism is warranted. The broader economic climate continues to present some uncertainties and hints towards a possible economic slowdown. Early warning signs include trade wars, a global slowdown, and sharp fluctuations in the stock market. Job growth was strong in June 2019, but future growth is expected to be slower. GDP growth came in close to expectations in second quarter (ending June 2019), due to consumption supported by rising incomes and high household confidence. However, manufacturing output declined in the second quarter as did business fixed investment. Core inflation continues to be less than targeted (2.0%).

Other factors

In the face of challenges from natural disasters and aging infrastructure, the Port and the City have made resiliency a key strategic goal. The Port's three-mile Embarcadero Seawall, constructed over 100 years ago, is the foundation of the City's edge, protecting businesses, utility and transportation infrastructure and critical emergency and disaster response facilities. With the threat of earthquakes and predicted sea level rise, the City must upgrade the Seawall so that it continues to function today and for generations to come. Since 2017, the Port and City have committed significant resources to advance technical studies and engineering feasibility of Seawall repairs, engage stakeholders and the public in decision-making, and seek project funding.

Embarcadero Seawall Program. The seawall and adjoining marginal wharf that run along the Embarcadero from Fisherman's Wharf to Mission Bay constitute the City's primary flood control system along the northern and central waterfront. A 2016 earthquake vulnerability study indicated that the waterfront is highly susceptible to earthquake damage associated with seawall movement and localized failure of the bulkheads. The Embarcadero Seawall Program is a major City and Port effort to improve seismic performance of the Embarcadero Seawall, provide near-term flood protection improvements, and plan for long-term resilience and sea level rise adaptation. These infrastructure improvements are estimated to cost up to \$5 billion over a 20 to 30-year period. The \$500 million Phase I of the Seawall Program will develop and complete the most immediate life safety, emergency response and flood risk improvements to the Seawall at key locations by approximately 2026. In November 2018, 83 percent of City voters approved a ballot measure authorizing bonded debt of \$425 million to support Phase I of the Seawall Program. The City and the Port continue to seek other sources of revenue, including state and federal support as well as local special taxes, to fully fund both Phase I and the subsequent phases of the Seawall Program.

Sea Level Rise. The Port currently experiences localized flooding due to higher water levels and settlement in certain areas. The shoreline from Pier 22 to Pier 9 includes some of the lowest elevations in San Francisco and these areas flood during king tides and storm events. The current 100-year flood event would

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result in the bay overtopping the Embarcadero Seawall at localized areas that are lowest along the shoreline. Due to the elevation of the land behind the shoreline, additional flooding over the 100-year flood event of an additional two to three feet would result in reaching a threshold that would result in flooding of significant citywide transportation and utility assets. Data from the San Francisco tidal gauge shows that the San Francisco Bay rose over eight inches between 1900 and 2000. Most of the bay shoreline, including San Francisco, consists of filled land that was elevated just high enough to avoid flooding at the time that the fill was placed. As a result, much of the shoreline is low relative to the bay and, as sea levels rise, the bay shoreline will experience more flooding over larger areas of land at longer durations. In 2018 the State of California adopted new sea level rise guidance and the San Francisco Capital Planning Committee adopted the new guidance in September 2019. The guidance includes two greenhouse gas emissions scenarios—representative concentration pathways or RCP 4.5 which assumes global emissions peak in 2040 and then decline and RCP 8.5 which assumes that global greenhouse gas emission continues to rise over the next century. The range of sea level rise scenarios for RCP 4.5 in 2030 are: 6 to 10 inches, 13 to 23 inches in 2050, 20 to 39 inches in 2070, and 33 to 71 inches in 2100. The ranges adopted for RCP 8.5 are: 6 to 10 inches in 2030, 13 to 23 inches 2050, 24 to 45 inches in 2070 and 41 to 83 inches in 2100. While these ranges are significant, it is important to recognize that sea level rise of only 16 inches on top of a 100-year flood event will impact Port facilities. A rise of over 50 inches would cause frequent flooding of the majority of the Port's facilities including the Embarcadero waterfront roadway. To meet this challenge, the Port has initiated or participated in several projects and programs, including the Embarcadero Seawall Program, a flood study with the US Army Corps of Engineers, the Citywide Sea Level Risk Vulnerability and Consequences project and the Citywide Hazard and Climate Resilience Plan. Additionally, the development projects occurring on Port property will implement protections against sea level rise.

Ten-year capital plan. City Administrative Code Section 3.20 requires the City to produce a Ten-Year Capital Plan (Capital Plan) that is updated every two years, alternating with the City's current biennial budget process. The Capital Plan distinguishes between renewal work and enhancements. Renewal work returns an existing facility to its original state of good repair whereas enhancements improve or increase asset performance. The most recent version of the Capital Plan, adopted by the Port Commission in February 2019 ("2020-2029 Capital Plan"), identifies \$3.5 billion in capital investments, including \$1.7 billion needed to fund deferred maintenance and subsystem renewals on Port facilities. This amount represents the anticipated cost over the next ten years to maintain Port facilities in a state-of-good-repair. The Port uses facility condition surveys to identify and prioritize maintenance projects that preserve and extend the economic life of the Port's productive assets. The 2020-2029 Capital Plan identifies an additional \$1.9 billion for enhancement projects. The enhancement category includes \$484.1 million for the Seawall Program, \$584.2 million for conditional seismic work, and \$786.4 million for other improvements.

The Port's need for capital investments has historically outpaced available funding. The Port has applied a multi-pronged approach to this challenge including dedicating funding to capital; securing new external sources of funding; and targeting available funds to strategic projects. The 2020-2029 Capital Plan identifies \$1.7 billion in available funding sources during the ten-year period. The anticipated sources include a mix of Port capital funds, private sector development project funding, City general obligation bond proceeds for parks and open space and the Embarcadero Seawall, tenant contributions pursuant to improvement and maintenance obligations required under existing leases, and federal, state and local grants.

Development projects continue to be a significant driver for certain waterfront improvements. The current capital plan projects \$757.4 million in development project funding over the ten-year period supported by a mix of public and private sources.

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The Port has worked to commit more internal resources to address capital requirements. In 2012, the Port Commission adopted a capital budget expenditure funding policy that both designates a minimum percentage set aside of annual operating revenues to fund capital projects and allocates one-time and surplus revenues to capital expenditures. Pursuant to this, the Port now designates a minimum of 25% of operating revenue each year in its operating budget to fund capital expenditures. The Port's budget has met or exceeded its capital funding target every year since adopting the capital funding policy and the Port anticipates meeting the specified threshold funding level in each of the ten years captured in the Capital Plan.

The plan projects that at the end of the ten-year period, the Port will have invested \$1.7 billion to fund both renewals and enhancements, leaving a backlog of \$1.2 billion for renewal work. The backlog consists of projects for which the Port (1) does not currently have sufficient funds to cover the estimated costs to repair and renew the facility, and (2) has not issued a request for proposals (RFP) or entered into negotiations with a developer to finance the upgrades. The Port has several options available to fund unmet needs: new public-private partnership development projects, new Port debt, general obligation bonds, grant opportunities, and infrastructure financing districts. Each new funding option requires substantial staff time to develop and implement, as well as support from policy makers. These financing tools may also require the support of regulatory bodies such as the California State Lands Commission and the San Francisco Bay Conservation and Development Commission.

Legislative efforts. Since 2005, the Port has pursued state and local legislative changes to increase the options available to fund the Port's future capital requirements and to expand the range and profitability of uses on Port property. The Port's current federal and state legislative program focuses on securing funding for the Seawall Program and shoreline improvements to enhance resilience and address sea level rise. The Port has successfully obtained authority to: (1) capture the state and local share of certain property tax increment revenues that would otherwise be paid to the state and local entities, and (2) form Infrastructure Finance Districts (IFDs) and issue IFD bonds against incremental property tax revenues to finance the public portion of several public-private development projects. Legislative efforts to support the Seawall Program include the approval of the Seawall Bond in November 2018 and the award of a \$5 million grant from the California Department of Natural Resources in February 2019.

In 2005, the California Legislature approved Senate Bill 1085 allowing the City and the Port to create IFDs in the Port area. IFDs help public agencies finance public infrastructure improvements by capturing and bonding against tax increment revenue generated in a district after it is established. Among other things, the State authorized the use of an IFD for urban waterfront areas in addition to undeveloped or underdeveloped areas; specifically clarified that publicly-owned property subject to tidelands trust for commerce, navigation and fisheries (the public trust), including filled tidelands, may be included in such districts; and enumerated additional examples of infrastructure improvements that qualify for IFDs, including seismic upgrades, historic renovation, environmental remediation, utility improvements, and structural repair or construction of seawalls, piers and wharves.

In June 2012, the Board of Supervisors approved an amended Resolution of Intention to establish Infrastructure Financing District No. 2 consisting of the entire waterfront area under Port jurisdiction, called the Port Area, and designated eight initial proposed project areas within this IFD. In June 2013, the Board of Supervisors adopted by resolution the "Guidelines for the Establishment and Use of Infrastructure Financing Districts on Project Areas on Land under Jurisdiction of the San Francisco Port Commission." In November 2015, the Board of Supervisors adopted a second amendment to the Resolution of Intention to Establish IFD under which the City declared its intention to establish Sub-Project Area G-1 (Pier 70 - Historic Core) within the Pier 70 district. Following all the necessary public process and proceedings and

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by passage of Ordinance No. 27-16 in March 2016, the Board of Supervisors formed and established the IFD and approved the related Infrastructure Financing Plan for the City and County of San Francisco Infrastructure Financing District No. 2 (Port of San Francisco). The activation of project or sub-project areas within the contemplated Port IFD will occur as entitled development activities progresses. The following have been activated: Sub-Project Area G-1 (Pier 70 – Historic Core) by Ordinance No. 27-16; Project Area I (Mission Rock) and Sub-Project Areas I-1 through I-13 by Ordinance No. 34-18; and Sub-Project Areas G-2, G-3 and G-4 (Pier 70) by Ordinance No. 220-18.

The Port and its development partners seek to take full advantage of special use district financing tools to fund necessary public infrastructure and make development projects feasible. In addition to IFDs, the infrastructure financing plans for certain Port development projects contemplate the formation and implementation of community facility districts (CFDs). A community facility district is an area that the City will establish in accordance with the City's CFD ordinance within which special taxes are levied to fund certain capital improvements and provide allowed services, consistent with the state Mello-Roos Act. Formal legislation by the Board of Supervisors is required to form a CFD. Formation and implementation of community facility districts for both the Pier 70 Area and Mission Rock (Seawall Lot 337 and Pier 48) development areas are planned for the second half of Fiscal Year 2019-20. Specifically, the Port plans to form Special Tax District 2020-1 (Pier 70 Leased Properties CFD) and Special Tax District 2020-2 (Pier 70 Condominiums CFD) in mid-Fiscal Year 2019-20. The Port plans to form a CFD Special Tax District at the Mission Rock site in the third or fourth quarter of Fiscal Year 2019-20.

Referendum and initiative processes. In the last five years, several local ballot measures have affected waterfront development. In November 2013, City voters passed a referendum overturning a June 2012 decision of the Board of Supervisors to allow the construction of a proposed high-rise residential development along the Embarcadero including the Port's Seawall Lot 351. A referendum is a petition protesting an ordinance passed by the Board of Supervisors and asking that the Board of Supervisors reconsider the matter. If the Board does not repeal the ordinance, it is submitted to the voters at the next general municipal election or a special election. The 2013 referendum reversed an increase in building height granted to the development by earlier City approvals. As a result of the referendum and litigation related to the project's certification under the California Environmental Quality Act (CEQA), the project at Seawall Lot 351 did not occur. The Port continues to operate Seawall Lot 351 under a license agreement to provide parking for the Ferry Building and other visitors to the waterfront.

City voters may also avail themselves of the initiative process, whereby a proposal for a new ordinance or charter amendment is placed on the ballot by a petition with the required number of signatures. The Port's properties were the subject of Proposition B passed by the San Francisco electorate on June 3, 2014. Proposition B requires voters' approval prior to any development on Port property that exceeds the height limits in effect as of January 1, 2014. Proposition B applies to property currently under the control of the Port Commission, as well as any property that the Port may acquire in the future. Proposition B requires that any future ballot question to increase height limits on Port property must specify both the existing and proposed height limits. Two development projects on Port property have become subject to the requirements of Proposition B. The developer of the Pier 70 Waterfront Site, through ballot measure Proposition F, received voter approval for its project's increase in height limits on November 4, 2014. The developer for a second project, Mission Rock, received voter approval for its project's increase in height limits through Proposition D on November 3, 2015. Both projects have secured initial entitlements and are now approved, and the Pier 70 Waterfront Site is under construction.

Waterfront Land Use Plan. The Port of San Francisco's Waterfront Land Use Plan (Waterfront Plan) establishes land use and urban design policies applicable to the waterfront properties under the Port's

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jurisdiction. The Port Commission initially adopted the Waterfront Plan in 1997. The plan has enabled the Port Commission, the City and the community to jointly define locations for new public-private partnership projects along the waterfront. The Port commenced a three-year public process to update the Waterfront Plan in 2015. A Waterfront Plan Working Group, assisted by seven specialty advisory teams, developed 161 Port-wide policy recommendations concerning how the Port should update its policies on land use, open space, maritime, transportation, environmental and waterfront resilience. Many recommendations call for new goals and policies and/or revisions to the 1997 Waterfront Plan. With the Port Commission's input and endorsement of the recommendations in August 2018 (Resolution No. 18-45), Port staff prepared the Draft Waterfront Plan, in June 2019. The Draft Plan is a comprehensive update which sets nine goals and supporting policies to guide the Port's work to make the waterfront more resilient, and promote improvements, including pier rehabilitation development projects in the Embarcadero Historic District. More information, including the Waterfront Plan Working Group's full report, can be found at <https://sfport.com/waterfront-plan-update>.

In July 2000, the Port and the San Francisco Bay Conservation and Development Commission (BCDC) agreed to amend the Port's Waterfront Plan and BCDC's San Francisco Bay Plan to create consistent plans for the waterfront area between the Hyde Street Pier and China Basin ("San Francisco Waterfront Special Area Plan"). Among other things, this amendment commits the Port to expend up to \$30 million over a twenty-year period for the removal of certain piers and the construction of major public plazas and other public access improvements. Since the amendment, the Port has expended \$46.6 million for projects under the Special Area Plan, including five pier removals (Piers ½, 24, 34, 36 and 64) and construction of the Brannan Street Wharf and the Cruise Terminal Plaza.

The 1997 Waterfront Plan identified several locations where mixed-use developments including maritime, open space and public access uses are encouraged. Such projects are generally undertaken as public-private partnerships, in which the Port enters into a development agreement and a long-term lease with a private developer, usually selected through a request for proposal process. Active development activities include:

Pier 70 Area

Pier 70 is approximately 69 acres, located on San Francisco's Central Waterfront, generally between 18th and 22nd Streets, east of Illinois Street. For over 150 years, some portion of the site has been in use for ship building and repair, steel production, and other supporting heavy industrial uses. In April 2014, the National Park Service approved the Port's nomination for the Union Iron Works Historic District at Pier 70 and listed the district in the National Register of Historic Places. As discussed in more detail in Note 17, the Port has completed an environmental investigation and risk assessment of the project area. Findings from the completed risk assessment do not indicate any immediate need for soil or groundwater remediation. Following a three-year community planning process, the Port Commission endorsed the Pier 70 Master Plan in May 2010. The plan balances sustained ship repair, historic preservation, new waterfront parks and new development. It identifies over three million square feet of new building potential and 700,000 square feet of buildings to be rehabilitated.

Historic Core – In February 2012, the Port Commission selected a developer and, in May 2012, entered into an exclusive negotiation agreement (ENA) for the lease, rehabilitation, and development of the Pier 70 20th Street Historic Buildings. The developer defined a use program of office, light industrial and commercial uses to revitalize the eight buildings in this project. In October 2012, the Port Commission endorsed a non-binding term sheet describing the fundamental deal terms for the project. The Board of Supervisors added its endorsement of the term sheet and found the proposed development fiscally feasible under the Administrative Code, Chapter 29 in December 2012. The Port and the developer executed the lease in July 2015. Construction of core and shell improvements commenced in August 2015 and the first

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completed building became available for occupancy in June 2017. One building remains under construction, with completion anticipated in 2020.

Waterfront Site – This project area requires significant infrastructure investment and land use approvals to redeploy a largely vacant portion of Pier 70 for new uses in new buildings, alongside three historic buildings that will be rehabilitated and adaptively reused. In May 2013, the Port Commission endorsed a non-binding term sheet describing the fundamental deal terms for the project. The Board of Supervisors endorsed the term sheet in June 2013 and determined the proposed development to be fiscally feasible under Chapter 29 of the Administrative Code. The passage of Proposition F in 2014 allowed a 90-foot height limit for the site. The land use program for the Waterfront Site, as defined within the proposed Pier 70 Special Use District amendments to the Planning Code, allows for the development of approximately 1,100 to 2,150 new residential units, and between one million and two million gross square feet of commercial and office space, as well as small-scale manufacturing, retail, neighborhood services, waterfront parks and public infrastructure. Necessary project entitlements, including certification of the Final Environmental Impact Report, were secured in fall 2017. Following the close of the master lease, the master developer commenced site preparation in May 2018 for Phase 1 of the project. Phase 1, expected to take four to six years to complete, includes the construction of infrastructure, extension of the street grid, new parks and open space, and preparation of development pads that will result in the development of up to 720 residential units, 356,000 square feet of office, and 115,000 square feet of retail, arts, and light industrial space. In February 2019, Parcel K North was sold, representing the first transaction for vertical development under the Pier 70 Special Use District. In March 2019, the master developer commenced construction of utilities, roadways, and other horizontal infrastructure for Phase 1 of the Pier 70 mixed-use project. Completion of Phase 1 horizontal improvements is anticipated in 2022.

Crane Cove Park – Crane Cove Park will be a major new Blue Greenway waterfront park located in the Central Waterfront generally between 19th and Mariposa Streets east of Illinois Street, in the Union Iron Works National Historic District at Pier 70. Park features include interpretation of the historic slipway and gantry cranes, a grand entrance plaza, a large green, a public beach with access for human powered boats, landscaping, historic artifacts, and renovations to Building 49 including restrooms. The Port has phased project construction to expedite delivery. The first stage of park construction commenced in late 2016. On November 13, 2018, the Port Commission awarded a contract to complete the majority of park construction including hardscape, irrigation and landscaping, site furnishings and construction of a beach. Park improvements and the 19th Street parking lot are nearly halfway complete. In-water work for beach construction began in June 2019 and the Port expects to complete the park project in 2020.

Seawall Lot 337 and Pier 48 (“Mission Rock”)

In 2010, the Port entered into an Exclusive Negotiation Agreement (ENA) with Seawall Lot 337 Associates, LLC for the mixed-use development of Seawall Lot No. 337 (SWL 337) and the adjacent Pier 48. Pursuant to the ENA, the developer submitted its revised proposal in 2012 which contemplates a flexible mixed-use development at the site, balancing residential, office, retail, exhibition and parking uses. The Port and the developer expect the combination of uses to evolve to meet market demands, reflect community and regulatory concerns, and ensure mixed-use diversity. The Port Commission and the Board of Supervisors endorsed a non-binding term sheet describing the fundamental negotiated elements and proposed financial terms for the lease and development of the project site in 2013. The Board of Supervisors also found the proposed development fiscally feasible under Chapter 29 of the Administrative Code. In 2014, the Port Commission approved an Amended and Restated ENA affording the developer additional time to accomplish the additional steps required as a result of Proposition B (June 2014). With the passage of Proposition D in 2015, the developer obtained voter approval of the project's proposed maximum building

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heights. The project secured necessary approvals in 2018 from the Port Commission, the Board of Supervisors and the State Lands Commission and received Bay Conservation and Development Commission permit approval in June 2018. Transaction documents, including the disposition and development agreement and financing plan for the fully entitled project, were executed in August 2018, and the Port Commission approved the Phase 1 budget in September 2019. Horizontal construction is anticipated to commence with Phase 1 vertical construction starting in 2020.

Fire Station #35 Expansion at Pier 22½

The Pier 22½ Fire Station #35 (FS 35) expansion project will improve the City's capacity for meeting current and future fire service demands, including water-oriented emergency response. The project concept consists of construction of a new two-level, approximately 15,000 square feet fireboat station behind the existing historic fire station. The new structure will rest on a new floating pier secured by pilings. A ramp located south of the existing FS 35 will provide access to the new firehouse from The Embarcadero. There is a pedestrian gangway between the two buildings. The new pier will provide berths for three fire boats and multiple small watercraft. The 2014 Earthquake Safety and Emergency Response bond provides funding for construction of this new and expanded facility. Construction commenced in fall of 2019.

Alcatraz Embarkation

The Pier 31½ marginal wharf is currently the embarkation point for visitors to Alcatraz Island, a major tourist destination run by the National Park Service (NPS). NPS and its partner, the Golden Gate National Parks Conservancy, and the Port are working together to transform the site, which was constructed for relatively short-term use, into a first-class embarkation site leasable for up to 50 years. The long-term designation of the site as the entry to Alcatraz facilitates a significant investment, to create a high-quality visitor amenities and interpretation. The proposed project includes: (1) renovation of the interiors of the Piers 31 and 33 bulkheads (approximately 18,000 square feet of gross leasable area); (2) improvements to 43,000 square feet of marginal wharf for a pedestrian-only area with public open space, passenger queueing, and site circulation; (3) addition of a second float to increase ferry capacity; (4) improvements to 13,200 square feet of support, storage, and parking area within the Pier 31 and Pier 33 sheds; and (5) repairs to the substructure of the Pier 31½ marginal wharf. The Port Commission and the Board of Supervisors endorsed a term sheet for the project in 2016. The Port Commission approved entitlements and transaction documents in June 2018 and the Board of Supervisors approved the project in September 2018. Construction will be phased, with multiple parties performing the work under different leases with different start dates. Repairs and improvements to the substructure of Pier 31½ and adjacent apron structures were largely completed in 2019. The schedule anticipates completion of all improvements by 2024.

Seawall Lot 322-1 Development for Affordable Housing (88 Broadway)

In 2014, the Port Commission approved a memorandum of understanding between the Port and the Mayor's Office of Housing and Community Development (MOHCD) to explore the feasibility of developing Seawall Lot 322-1 with affordable housing. Port staff secured enabling state legislation that added this site to designated seawall lots that may, under specified conditions, be leased for non-trust uses, including affordable housing. MOHCD selected a private development partner in August 2016. The project will include approximately 124 affordable housing units and one manager unit totaling approximately 137,100 gross square feet of residential dwelling space and approximately 8,700 gross square feet of nonresidential space. Residents will have access to a common, community room on the ground floor, an open podium courtyard on the second floor, two open decks on the fifth and sixth floors, and a rooftop terrace and community garden. Ancillary ground-level uses could include retail/commercial, a childcare center with an outdoor play area, and a childcare arcade. The Port Commission and the Board of Supervisors approved the project in July 2018. Construction commenced in 2019 with anticipated occupancy in 2021.

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Seawall Lots 323 and 324

In 2015, the Port Commission approved an ENA with Teatro ZinZanni and a financial partner, operating together as TZK Broadway, LLC, for the lease and development of Seawall Lots 323 and 324 for a dinner-theater, a maximum 200-room, 40-foot high boutique hotel and an approximately 14,000-square foot privately-financed public park, and ancillary uses. The Port Commission and the Board of Supervisors both endorsed a non-binding term sheet for the project in 2016. The development team has added a financial partner, is working to secure project entitlements, and anticipates construction to commence in 2020 with completion in 2022.

Downtown Ferry Terminal Expansion

The San Francisco Bay Area Water Emergency Transportation Authority (WETA) is expanding and improving facilities at the existing ferry terminal in downtown San Francisco. The project will add ferry gates, improve pedestrian circulation and ferry patron boarding, enhance emergency response capabilities, and accommodate anticipated increases in ferry ridership. The project includes construction of two new ferry gates (Gates F and G) and four new berths, landside pedestrian circulation improvements, installation of amenities such as weather-protected areas for queuing and covering of the current "lagoon" area south of the Ferry Building. This covered area will enhance emergency response capabilities and serve as a new public plaza in the heart of the Ferry Building area, supporting passenger queuing, markets, and public use. The new gates and amenities will support new ferry service to Richmond, Treasure Island, and other locations, as well as efforts to enhance existing services. As part of this project, WETA will also refurbish and assume control of the adjacent Gate E. Project construction commenced June 2017. In 2019, WETA opened the two new gates and plans to open the third gate and public plaza in 2020.

Mission Bay Ferry Landing

The proposed Mission Bay Ferry Landing will provide regional ferry service to and from San Francisco's Mission Bay, Dogpatch, Potrero Hill, Pier 70, and Central Waterfront neighborhoods. The ferry landing will provide capability to berth two ferry boats simultaneously and may include a nearby water taxi landing. This ferry terminal will have the capacity to handle up to 6,000 passengers per day. The terminal is essential to alleviate current regional transportation overcrowding and provide transportation resiliency in the event of an earthquake, BART or Bay Bridge failure, or other unplanned events. The Port is leading the project in collaboration with WETA, with the support of the Mayor's Office, Office of Economic and Workforce Development, and consulting design teams. The project design is completed. The Port is soliciting proposals for construction and a contract is expected to be awarded in spring 2020. The Port anticipates receiving environmental permits in early calendar year 2020. The Port expects construction to commence in summer 2020 with substantial completion in later calendar year 2021. Funding is nearly secured, however litigation challenging Regional Measure 3, a major source of funds for the project, could delay construction. In the meantime, the Port and WETA installed an interim ferry landing at Pier 48½ with financial support from Golden Gate Transit which opened in fall 2019.

Park projects

The City's ten-year capital plan programs periodic general obligation bond measures for park projects. Since 2008 the Port has received funding from two parks bond issues, \$34.5 million from the 2012 bond measure and \$33.5 million from the 2008 measure. Port projects funded by the 2012 bond issue include the Cruise Terminal Plaza fronting the James R. Herman Cruise Terminal at Pier 27, Agua Vista Park, Crane Cove Park, improvements to Islais Creek and Heron's Head Park. The 2008 bond issue funded projects including a promenade at Pier 43½ in Fisherman's Wharf, the Brannan Street Wharf Park; Bayfront Park, Crane Cove Park, Islais Creek, Bayview Gateway, and improvements to Heron's Head Park. Through June 30, 2019, the Port has expended approximately \$80.2 million for park projects, including \$51.3 million from the park bonds and \$28.9 million from other funds.

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Requests for Information

This report is designed to provide a general overview of the Port of San Francisco's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Public Information Officer at Port of San Francisco, Pier 1, San Francisco, California, 94111. Additional information concerning the Port can also be found at www.sfport.com. Questions concerning the City and County of San Francisco or requests for a copy of the City's Comprehensive Annual Financial Report should be addressed to: Office of the Controller, City and County of San Francisco, City Hall, Room 316, 1 Dr. Carlton B. Goodlett Place, San Francisco, California 94102. Additional information concerning the City can also be found at www.sfgov.org.

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Statements of Net Position
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(dollar amounts in thousands)

	2019	2018
Assets		
Current assets:		
Unrestricted:		
Cash and investments held in City Treasury (Note 3)	\$ 158,208	\$ 155,722
Cash held outside of City Treasury (Note 3)	5	5
Receivables, net (Note 4)	13,985	12,060
Due from other City funds (Note 14)	14,958	-
Accrued interest receivable	1,299	699
Materials and supplies	1,348	1,352
Prepaid charges and advances (Note 5)	114	-
Total unrestricted current assets	189,917	169,838
Restricted:		
Cash and investments held in City Treasury (Note 3)	26,042	30,877
Cash and investments held outside of City Treasury (Note 3)	8,779	10,077
Total restricted current assets	34,821	40,954
Total current assets	224,738	210,792
Noncurrent assets:		
Capital assets (Note 6):		
Nondepreciable	132,749	130,380
Depreciable, net	331,523	304,322
Capital assets, net	464,272	434,702
Unrestricted other noncurrent assets (Note 7)	2,731	3,300
Advance to other City funds (Note 14)	350	332
Total noncurrent assets	467,353	438,334
Total assets	692,091	649,126
Deferred outflows of resources		
Deferred outflows of resources related to pension (Note 10)	12,023	12,986
Deferred outflows of resources related to other postemployment benefits (OPEB) (Note 12)	2,524	1,686
Total deferred outflows of resources	14,547	14,672

The accompanying notes are an integral part of these financial statements.

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Statements of Net Position (Continued)

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(dollar amounts in thousands)

	2019	2018
Liabilities		
Current liabilities:		
Accounts payable and accrued expenses	\$ 7,464	\$ 9,551
Due to other City funds (Note 14)	585	-
Accrued interest payable	1,740	1,535
Accrued payroll	1,654	1,667
Accrued vacation and sick leave pay (Note 8)	1,362	1,346
Accrued workers' compensation (Notes 8 and 18)	417	454
Estimated claims payable (Notes 8 and 18)	200	200
Current maturities of long-term obligations (Note 8)	3,079	2,693
Pollution remediation obligations (Notes 8 and 17)	44	44
Prepaid rents and advance payments	3,058	4,077
Rent credits due to tenants	2,559	1,986
Lessee and other deposits	9,763	8,668
	31,925	32,221
Noncurrent liabilities:		
Accrued vacation and sick leave pay (Note 8)	957	909
Accrued workers' compensation (Notes 8 and 18)	2,131	2,546
Estimated claims payable (Notes 8 and 18)	250	250
Long-term obligations - net of current maturities (Note 8)	86,625	83,622
Pollution remediation obligations (Notes 8 and 17)	4,105	3,000
Net pension liability (Note 10)	38,027	43,730
Net OPEB liability (Note 12)	28,956	30,750
Prepaid rents, advance payments and other liabilities	28,095	13,981
Rent credits due to tenants	45,020	47,636
	234,166	226,424
Total liabilities	266,091	258,645
Deferred inflows of resources		
Deferred inflows of resources related to pensions (Note 10)	7,224	3,151
Deferred inflows of resources related to OPEB (Notes 12)	2,685	50
	9,909	3,201
Net position		
Net investment in capital assets	334,188	305,609
Restricted for capital projects	14,467	20,738
Unrestricted	81,983	75,605
	\$ 430,638	\$ 401,952

The accompanying notes are an integral part of these financial statements.

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**PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
PORT OF SAN FRANCISCO**

Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended June 30, 2019 and 2018
(dollar amounts in thousands)

	2019	2018
Operating revenues (Note 9):		
Commercial and industrial	\$ 60,034	\$ 57,336
Parking	21,793	22,281
Cruise	7,947	7,901
Cargo	7,843	8,685
Fishing	2,273	2,184
Harbor services	2,672	1,847
Other maritime	2,559	2,652
Other	16,912	6,883
Total operating revenues	122,033	109,769
Operating expenses:		
Personal services	37,905	40,930
Contractual services	19,129	18,038
Utilities	2,961	2,859
Materials and supplies	1,353	1,001
Depreciation and amortization	24,608	17,778
General and administrative	3,847	3,585
Services provided by other City departments (Note 14)	18,718	19,310
Pollution remediation (Note 17)	1,105	(8,211)
Other	2,482	1,514
Total operating expenses	112,108	96,804
Operating income	9,925	12,965
Nonoperating revenues (expenses):		
Interest and investment income	6,189	2,231
Operating grants and transfers	3,331	4,232
Dispositions, net	(174)	(1,383)
Interest expense	(4,334)	(4,461)
Other contributions (Note 6)	(6,500)	-
Total net nonoperating revenues (expenses)	(1,488)	619
Change in net position before capital contributions and special item	8,437	13,584
Capital contributions:		
Grants from government agencies and other contributions	1,909	2,626
Special item:		
Receipt of operations - South Beach Harbor (Note 13)	18,340	-
Change in net position	28,686	16,210
Net position, beginning of the year, as previously reported	401,952	389,740
Cumulative effect of change in accounting principle due to implementation of GASB 75 (Note 2)	-	(3,998)
Net position, beginning of the year, as restated	401,952	385,742
Net position, end of the year	\$ 430,638	\$ 401,952

The accompanying notes are an integral part of these financial statements.

**PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
PORT OF SAN FRANCISCO**

Statements of Cash Flows
For the Years Ended June 30, 2019 and 2018
(dollar amounts in thousands)

	2019	2018
Cash flows from operating activities:		
Cash received from tenants for rent	\$ 81,496	\$ 78,499
Cash received from customers and others	37,994	30,794
Deposits received from tenants and customers	1,632	608
Cash paid to employees for services	(38,534)	(38,631)
Cash paid to suppliers for goods and services	(32,417)	(25,936)
Cash paid to City for services	(19,154)	(19,345)
Customer deposits returned	(612)	(364)
Net cash provided by operating activities	30,405	25,625
Cash flows from noncapital financing activities:		
Contribution from other City Departments	500	4,250
Operating grants	48	730
Proceeds from OCII related to South Beach Harbor operations (Note 13)	5,078	-
Other contribution (Note 6)	(6,500)	-
Net cash provided by noncapital financing activities	(874)	4,980
Cash flows from capital and related financing activities:		
Acquisition and construction of facilities and equipment	(32,924)	(15,498)
Dredging	(2,565)	(4,920)
Payments of long-term debt	(2,693)	(2,567)
Interest payments on long-term debt	(4,463)	(4,587)
Capital grants and contributions received	3,980	993
Proceeds from sale of equipment and materials	14	30
Net cash (used in) capital and related financing activities	(38,651)	(26,549)
Cash flows from investing activities:		
Interest and investment income	5,465	1,709
Net cash provided by investing activities	5,465	1,709
Change in cash and cash equivalents	(3,655)	5,765
Cash and cash equivalents, beginning of year	196,416	190,651
Cash and cash equivalents, end of year	\$ 192,761	\$ 196,416

The accompanying notes are an integral part of these financial statements.

**PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
PORT OF SAN FRANCISCO**

Statements of Cash Flows (Continued)
For the Years Ended June 30, 2019 and 2018
(dollar amounts in thousands)

	<u>2019</u>	<u>2018</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 9,925	\$ 12,965
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	24,608	17,778
Change in allowance for doubtful accounts	2,212	(180)
Net effects of (increase) decrease in:		
Receivables	(3,322)	763
Tenant deposits held outside City Treasury	(8)	-
Materials and supplies	4	240
Prepaid charges, advances and other assets	854	428
Advance to other City funds	(350)	-
Net effects of increase (decrease) in:		
Accounts payable and accrued expenses	(844)	1,580
Payable to other City funds	585	-
Accrued payroll	(13)	55
Accrued vacation and sick leave pay	64	88
Accrued workers' compensation	(452)	94
Estimated claims payable	-	(675)
Pollution remediation obligations	1,105	(8,398)
Net OPEB liability and related deferred outflows/inflows of resources	3	1,252
Rent credits, prepaid rent and other liabilities	(3,299)	(1,358)
Net pension liability and related deferred outflows/inflows of resources	(667)	993
Net cash provided by operating activities	<u>\$ 30,405</u>	<u>\$ 25,625</u>
Noncash capital and related financing activities:		
Acquisition of capital assets in accounts payable and accrued expenses	\$ 3,790	\$ 5,033
Tenant improvements financed by rent credits	90	2,590
Capitalized interest	64	18
Asset disposals and abandoned capital improvement projects	(188)	(1,413)
Capital assets transferred from OCII	19,966	-
Debt assumed from OCII	(6,144)	-
Reconciliation of cash and equivalents to the statement of net position:		
Cash and investments held in City Treasury		
Unrestricted	\$ 158,208	\$ 155,722
Restricted	26,042	30,877
Cash and investments held outside City Treasury		
Unrestricted	5	5
Restricted	8,779	10,077
Cash and equivalents	<u>193,034</u>	<u>196,681</u>
Less: Investment outside of City Treasury not meeting the definition of cash equivalents	<u>(273)</u>	<u>(265)</u>
Total cash and cash equivalents	<u>\$ 192,761</u>	<u>\$ 196,416</u>

The accompanying notes are an integral part of these financial statements.

PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
PORT OF SAN FRANCISCO
Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

1. Organization

The Port of San Francisco (Port) is an enterprise fund of the City and County of San Francisco (City). Only the accounts of the Port are included in these financial statements. There are no component units that should be considered for inclusion in the Port's financial reporting entity. A five-member Port Commission is responsible for the organization's operation, development, and maintenance. Commission members are appointed by the Mayor and confirmed by the Board of Supervisors for fixed terms of four years. The Port is a department of the City, and the accompanying financial statements are included in the City's basic financial statements.

Prior to February 1969, the Port was owned and administered by a state agency, the San Francisco Port Authority. In February 1969, the State of California (State) transferred the Port in trust to the City under the terms and conditions specified in the State statutes of 1968, Chapter 1333 (Burton Act), as amended, and ratified by the City's voters in November 1968. Under the terms of the Burton Act, the State Legislature reserves the right to amend, modify, or revoke, in whole or in part, the transfer of lands in trust, provided that the State would then assume all lawful obligations related to such lands.

The Port's revenue is derived primarily from property rentals to commercial and industrial enterprises and from maritime operations, which include cargo, ship repair, fishing, harbor services, cruise and other maritime activities. Substantially all of the Port's property rental customers are located within the boundaries of the City. Port revenues are held in a separate fund (Harbor Fund) and are appropriated for expenditure pursuant to the budget and fiscal provisions of the City Charter, consistent with trust requirements. Under public trust doctrine, the Burton Act, and the transfer agreement between the City and the State, these revenues may be spent only for uses and purposes of the public trust.

2. Significant Accounting Policies

Basis of Accounting

The Port's financial statements are prepared using the economic resources measurement focus and the accrual basis in accordance with generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board (GASB). Under the accrual basis of accounting, revenues are recorded when earned and expenses are recorded when a liability is incurred. The statement of net position presents the residual difference between (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources as the net position. Net position is reported in three broad components, as applicable – net investment in capital assets; restricted; and unrestricted. Under the all-inclusive approach to presenting the changes in net position, all Port revenues, including capital contributions, are reported in the statement of revenues, expenses and changes in net position.

Cash Equivalents

The Port considers highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. The Port's cash and investments in the City Treasury are, in substance, demand deposits and are considered cash equivalents.

PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
PORT OF SAN FRANCISCO
Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

2. Significant Accounting Policies (Continued)

Investments

The Port reports its investments at fair value in the accompanying financial statements and the corresponding change in fair value of investments is reported in the year in which the change occurs. Money market investments with a remaining maturity at the time of purchase of one year or less are valued at amortized cost.

Fair Value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is a market-based measurement, using observable market transactions or available market information.

Restricted Cash and Investments

Assets whose use is restricted to specific purposes by bond indenture or otherwise are segregated on the statement of net position. These assets are primarily restricted for construction and debt service purposes. Bond interest and redemption represent funds accumulated for debt service payments due in the next twelve months and reserve funds set aside to make up potential future deficiencies. A bond trustee holds these funds.

Cash security deposits received by the Port pursuant to lease agreements are held in the City Treasury. Other lessee deposits are renewable certificates of deposit tendered by tenants in lieu of cash and held by banks as third-party certificates in the name of the Port.

Capital outlay funds are restricted for use in construction and acquisition of equipment, due to restrictions from grant agreements and bond resolutions. It is Port policy to first apply restricted resources when both restricted and unrestricted resources are available to cover the expenditure.

Materials and Supplies

Materials and supplies are used for construction and maintenance of Port facilities and are stated at average cost.

Capital Assets

Land transferred to the City in February 1969 is stated at an amount which includes an increase over the historical cost of \$56,063,000. This amount was recorded by the State to reflect appraised values in 1929 and carried forward in the accounting records transferred to the City.

Capital assets purchased are stated at cost. It is the policy of the Port to capitalize all expenditures of more than \$100,000 for infrastructure and facilities and improvements and \$5,000 for equipment and vehicles with an estimated useful life in excess of one year. Donated surplus equipment received from the federal government is carried at an acquisition value determined in accordance with federal guidelines. Interest paid on bond funds used for construction purposes, less interest earned on the temporary investment of the proceeds of such tax-exempt borrowings, if applicable, is capitalized from the date of borrowing through the construction period.

PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
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Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

2. Significant Accounting Policies (Continued)

Capital Assets (continued)

Depreciation and amortization expense are calculated using the straight-line method over the following estimated useful lives of the assets:

Facilities and improvements	5 to 65 years
Machinery and equipment	2 to 30 years
Infrastructure	15 to 40 years
Intangible assets	Varies with type

Tenant improvements are amortized using the straight-line method over the shorter of the estimated life of the asset or the remaining term of the related lease. Maintenance and repairs are expensed as incurred. Dredging costs are amortized using the straight-line method over the estimated useful period ranging from one to seven years. The Port's Waterfront Land Use Plan was approved in 1997. The costs of the plan are amortized using the straight-line method over an estimated life of 20 years.

Bond Premiums and Discounts

Bond premiums and discounts are amortized using the straight-line method over the life of the bonds. Bonds payable are recorded net of the applicable bond premium or discount.

Rent Credits

Rent credits are issued to certain tenants to finance certain facility improvements that are beneficial to the Port. Rent credits are recognized in accordance with the lease agreements by those tenants. Port facility improvements and related rent credit obligations, which apply against tenant minimum rents, are recorded by the Port and amortized over the leasehold period using the straight-line method.

Pollution Remediation Obligations

Pollution remediation obligations represent the accrued costs to address current or potential detrimental effects of existing pollution. These obligations are measured at their current value using a cost-accumulation approach, based on the pollution remediation outlays expected to be incurred to settle those obligations. Each obligation or obligating event is measured as the sum of probability-weighted amounts in a range of possible estimated amounts. Some estimates of ranges of possible cash flows may be limited to a few discrete scenarios or a single scenario, such as the amount specified in a contract for pollution remediation services.

Restricted Net Position

Restricted net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. A liability relates to restricted assets if the asset results from a resource flow that also results in recognition of a liability or if the liability will be liquidated with the restricted assets reported. Assets are considered restricted when constraints on consumption or use are imposed by third parties or enabling legislation.

PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
PORT OF SAN FRANCISCO
Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

2. Significant Accounting Policies (Continued)

Operating Revenues and Expenses

The Port distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from real estate leasing, maritime and other principal ongoing activities of the Port's normal business operations. Real estate revenues consist principally of rentals of Port property to industrial, commercial, retail, office and other business enterprises. Parking revenues include parking lot operations, metered on-street parking and parking fine revenue. Maritime revenues are derived from vessel operations, warehousing, harbor services and other maritime activities. Vessel operations include roll-on/roll-off ships for automobiles, dry, liquid bulk, and break-bulk cargoes, cruise, and other berthing. Other operating revenues include building permit and inspections fees. Operating expenses include facility maintenance, the cost of operations, administrative expenses, and depreciation and amortization on capital assets. Revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Minimum base rental revenue is recognized on the straight-line basis over related lease terms. Most term leases provide rents to be payable to the Port in equal monthly installments on the first day of each month until the termination of the lease. Contingent rentals are recorded or accrued only for periods in which thresholds for gross sales or revenues are met by the tenant. Use fees are recorded when the fee is earned, based on actual occupancy or use. Use fees are assessed by a measuring unit (e.g. lineal feet of the vessel for dockage) or measured time (e.g. per twenty-four-hour day). Maritime activity or use fees may be based on a standardized tariff schedule or covered by specific contractual agreements.

Capital Contributions

The Port, at various times, receives federal and state grants, proceeds from City general obligation bonds, and other funds from external sources for the construction of waterfront facilities and improvements. The funds are reported as capital contributions on the statement of revenues, expenses and changes in net position.

Special Item

Special items are significant transactions or events within the control of management that are either (1) unusual in nature (possessing a high degree of abnormality and clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the entity) or (2) infrequent in occurrence (not reasonably expected to recur in the foreseeable future, taking into account the environment in which the entity operates).

The Port received South Beach Harbor (SBH) operations and assets from the Office of Community Investment and Infrastructure (OCII) on May 1st, 2019. This transaction qualifies as a special item since this action was under the control of the Port's and OCII's Commissioners and met the criteria of infrequency (see Note 13).

Effects of New Pronouncements

In 2019, the City adopted GASB Statement No. 83, *Certain Asset Retirement Obligations* (GASB 83) and No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements* (GASB 88). GASB 83 establishes accounting and financial reporting standards for certain asset retirement obligations (AROs). The City's adoption of GASB 83 did not have a material impact on the Port's financial statements. GASB 88 establishes additional financial

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For the Years Ended June 30, 2019 and 2018

2. Significant Accounting Policies (Continued)

Effects of New Pronouncements (continued)

statement note disclosure requirements related to debt obligations of governments, including direct borrowings and direct placements. The Port adopted the provisions of this statement. Refer to Note 8 for details.

In 2018, the City implemented GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (OPEB) (GASB 75), which is intended to improve accounting and financial reporting for OPEB. GASB 75 identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service.

As of July 1, 2017, the Port restated its net position as follows:

Cumulative effect on Beginning Net Position as of July 1, 2017 (in thousands):

	<u>Increase/(Decrease)</u>
Beginning Net OPEB Liability pursuant to GASB 75	\$ (29,383)
Beginning Deferred Outflows of Resources pursuant to GASB 75	1,521
Remove Net OPEB Obligation, June 30, 2017	<u>23,864</u>
Total cumulative effect of change in accounting principle	<u><u>\$ (3,998)</u></u>

The City and the Port are currently analyzing their accounting practices to determine the potential impact on the financial statements of certain new accounting standards pronouncements issued by the GASB, including GASB Statement No. 84, *Fiduciary Activities*, GASB Statement No. 87, *Leases* (GASB 87), GASB Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, GASB Statement No. 90, *Majority Equity Interests*, and GASB Statement No. 91, *Conduit Debt Obligations*.

The Port anticipates that the implementation of GASB 87 will have a material impact on the Port's financial statements. GASB 87 establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under GASB 87, a lessor (like the Port) is required to recognize, for each lease, a lease receivable and a deferred inflow of resources. The lease receivable is measured at the present value of lease payments expected to be received during the term of the lease. The deferred inflow of resources is measured at the value of the lease receivable plus any payments received at or before the commencement of the lease term that relates to future periods. Interest revenue is recognized on the lease receivable and inflow of resources (revenue) is recognized from the deferred inflows of resources in a systematic and rational manner over the term of the lease. Lessors do not derecognize the asset underlying the lease. To allow adequate time for financial statement preparers to plan for the transition and its implementation, the accounting change for leases is required by the year ending June 30, 2021. For the transition, leases should be converted ("recognized and measured") using the facts and circumstances that exist at the beginning of the period of implementation, or the beginning of the earliest period restated.

PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO
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Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

2. Significant Accounting Policies (Continued)

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, deferred outflows of resources, liabilities, and deferred inflows of resources, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Cash and Investments

The Port's cash and investments at June 30, 2019 and 2018 are as follows (in thousands):

	2019	2018
Cash and investments in City Treasury	\$ 158,208	\$ 155,722
Cash outside of City Treasury - imprest fund	5	5
Restricted assets:		
Cash and investments in City Treasury	26,042	30,877
Cash and investments outside of City Treasury:		
Cash and investments held by fiscal agents	8,506	9,812
Lessee deposits	273	265
	\$ 193,034	\$ 196,681

City Treasurer's Pool

The Port maintains its operating fund cash and investments and a portion of its restricted asset cash and investments as part of the City's pool of cash and investments. The notes to the basic financial statements of the City provide more detailed information concerning deposit and investment risks and fair value hierarchy disclosure associated with the City's pool of cash and investments at June 30, 2019 and 2018. The City's pool is invested pursuant to investment policy guidelines established by the City Treasurer, subject to review by the Treasury Oversight Committee. The Treasury Oversight Committee, established under California Government Code Sections 27130 to 27137, is composed of various City officials and representatives of agencies with large cash balances. The objectives of the policy are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The provisions of the City's investment policy also address interest rate risk, credit risk, and concentration of credit risk and provides for additional restrictions related to investments.

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity period of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the City Treasurer manages its exposure to interest rate risk is by purchasing a combination of shorter-term and longer-term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash

PORT COMMISSION
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Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

3. Cash and Investments (Continued)

flow and liquidity needed for operations. The City’s investment policy specifies authorized investment types and sets parameters for maximum maturity.

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The City’s pool is not registered with the SEC as an investment company and is not rated.

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in possession of another party. The California Government Code, and the City’s investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for investments; however, it is the practice of the City Treasurer that all investments are insured, registered or held by the City Treasurer’s custodial agent in the City’s name.

To address concentration of credit risk, the City’s investment policy sets parameters pertaining to the maximum percentage of the total portfolio which may be invested in specific investment types and the maximum investment to one issuer for certain investment types. U.S. Treasury and Agency securities are not subject to this limitation.

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the City will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The California Government Code and the City’s investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the following provision for deposits. The California Government Code requires California banks and savings and loan associations to secure the City’s deposits not covered by federal deposit insurance by pledging authorized securities as collateral. The market value of pledged securities must equal at least 110 percent of the City’s deposits. The collateral must be held at the pledging bank’s trust department or another bank, acting as the pledging bank’s agent, in the City’s name. The investment policy states that mortgage-backed collateral will not be accepted. At June 30, 2019 and 2018, all of the banks with funds deposited by the Treasurer secure those deposits with sufficient collateral. The following table shows the maturity of the City’s pooled investments:

	<u>Investment maturities (in months)</u>			
	<u>Under 1</u>	<u>1-6</u>	<u>6-12</u>	<u>12-60</u>
FY 2019	17.4%	22.2%	16.3%	44.1%
FY 2018	14.3%	22.1%	18.5%	45.1%

At June 30, 2019 and 2018, the City’s pooled investments have a weighted average maturity of 1.28 years and 1.29 years, respectively.

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Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

3. Cash and Investments (Continued)

Cash and Investments Outside of City Treasurer’s Pool

Cash and investments outside of the City Treasurer’s Pool consist of cash, cash equivalents, money market mutual funds and U.S. agency securities. The Port categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The fair value hierarchy is based on the valuation inputs used to measure the fair value of the assets. Level 1 inputs are quoted prices in an active market for identical assets; Level 2 inputs are significant other observable inputs, and; Level 3 inputs are significant unobservable inputs. As of June 30, 2018, Port held \$2,825,000 U.S. agency securities using Level 2 input. The money market mutual funds are recorded at net asset value and seek to provide daily liquidity while maximizing current income. Commercial Paper at the time of purchase were within one year of their maturity dates and will mature by October 1st, 2019. They are recorded using the amortized cost method.

Investment classified in Level 2 of the fair value hierarchy is valued using prices determined by the use of matrix pricing techniques maintained by the various pricing vendors for these securities. Investments are priced based on evaluated prices, and such evaluated prices may be determined by factors which include, but are not limited to, market quotations, yields, maturities, call features, ratings, institutional size trading in similar groups of securities and developments related to specific securities.

At June 30, 2019 and 2018, cash equivalents and investments held by fiscal agents consisted of (in thousands):

	2019	2018
Reserve accounts:		
Cash equivalents - U.S. Bank commercial paper	\$ 3,909	\$ 3,972
Money market mutual fund	2,923	-
U.S. agency securities	-	2,825
Project account:		
Money market mutual fund	1,493	2,890
Debt service and other accounts:		
Cash equivalents - U.S. Bank commercial paper	181	125
	\$ 8,506	\$ 9,812

Investment of all funds and accounts held by trustees are governed by underlying trust documents, like the Bond Indenture (Indenture) and trust agreement for the Certificates of Participation (COP), rather than the general provisions of the California Government Code or the City’s investment policy.

A portion of the investments held by the bond trustee consists of the trustee bank’s open commercial paper (no term). The trustee bank’s commercial paper has a Standard & Poor’s rating of A-1+ and a Moody’s rating of P-1 at June 30, 2019 and 2018. The money market mutual fund has a Standard & Poor’s rating of AAAm and a Moody’s rating of Aaa-mf at June 30, 2019 and 2018. The U.S. government agency securities have a Standard & Poor’s rating of AA+ and a Moody’s rating of AAA as of June 30, 2018.

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CITY AND COUNTY OF SAN FRANCISCO
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Notes to Financial Statements
For the Years Ended June 30, 2019 and 2018

3. Cash and Investments (Continued)

Certain lessee security deposits are held on behalf of the Port by third party trustees and invested in renewable certificates of deposit. Deposits that are made by tenants directly to banks are held outside of the City Treasury and are not collateralized as public agency deposits.

4. Receivables

Receivables consisted of the following June 30, 2019 and 2018 (in thousands):

	<u>2019</u>	<u>2018</u>
Accounts receivable from tenants and customers	\$ 9,483	\$ 7,252
Less allowance for doubtful accounts	<u>(2,773)</u>	<u>(561)</u>
Accounts receivable, net	6,710	6,691
Grants receivable	2,789	2,077
Other	<u>4,486</u>	<u>3,292</u>
	<u>\$ 13,985</u>	<u>\$ 12,060</u>

Other receivables consist principally of cost recoveries due from others pursuant to development or other agreements.

5. Prepaid Charges and Advances

The Port and the United States Army Corps of Engineers (USACE) periodically enter into cost-sharing agreements for the USACE to carry out local work that is in the federal interest. Under these cost-sharing arrangements, the Port is typically required to pay an estimated cost share in advance to the USACE. Unexpended advances available to the USACE for the San Francisco Waterfront Flood Risk Resiliency Study were \$114,000 on June 30, 2019.

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6. Capital Assets

A summary of changes in capital assets for years ended June 30, 2019 and 2018 are as follows (in thousands):

	Balance July 1, 2018	Increases	Decreases	Receipt of operations South Beach Harbor (Note 13)	Balance June 30, 2019
Capital assets, not being depreciated/amortized:					
Land	\$ 104,169	\$ -	\$ 188	\$ -	\$ 103,981
Construction in progress	26,211	32,955	30,398	-	28,768
Total capital assets, not being depreciated/ amortized	<u>130,380</u>	<u>32,955</u>	<u>30,586</u>	<u>-</u>	<u>132,749</u>
Capital assets, being depreciated/amortized:					
Facilities and improvements	590,459	25,330	-	19,966	635,755
Machinery and equipment	25,834	3,948	468	-	29,314
Intangible assets	2,264	-	-	-	2,264
Dredging	9,460	2,565	-	-	12,025
Waterfront Land Use Plan	2,795	-	2,795	-	-
Infrastructure	30,682	-	-	-	30,682
Total capital assets, being depreciated/ amortized	<u>661,494</u>	<u>31,843</u>	<u>3,263</u>	<u>19,966</u>	<u>710,040</u>
Less accumulated depreciation/amortization for:					
Facilities and improvements	315,126	18,074	-	-	333,200
Machinery and equipment	16,739	1,419	468	-	17,690
Intangible assets	2,234	32	-	-	2,266
Dredging	6,081	3,647	-	-	9,728
Waterfront Land Use Plan	2,795	-	2,795	-	-
Infrastructure	14,197	1,436	-	-	15,633
Total accumulated depreciation/amortization	<u>357,172</u>	<u>24,608</u>	<u>3,263</u>	<u>-</u>	<u>378,517</u>
Total capital assets, being depreciated/amortized, net	<u>304,322</u>	<u>7,235</u>	<u>-</u>	<u>19,966</u>	<u>331,523</u>
Capital assets, net	<u>\$ 434,702</u>	<u>\$ 40,190</u>	<u>\$ 30,586</u>	<u>\$ 19,966</u>	<u>\$ 464,272</u>

The Pier 70 Mixed-Use District Project is a mixed-use development on the Port's central and southern waterfront areas. In October 2017, the Board of Supervisors approved the formation of the Pier 70 Special Use District (SUD) and a disposition and development agreement (DDA) with the Pier 70 developer. Under the terms of the DDA, the Port agreed to sell Parcel K North (PKN), a Port-owned parcel free from the public trust restrictions, to a developer. On February 13, 2019, the Port sold PKN to a developer in exchange for a promissory note of \$24,230,000. However, the execution of the promissory note and the resulting gain on the sale of PKN is contingent on the pending formation of the Pier 70 Community Facility District scheduled to be complete in fiscal year 2020. Accordingly, the Port wrote off the book value of the parcel and recognized a loss on disposal of \$188,000 in fiscal year 2019. The Port also made a \$6,500,000 contribution to the Pier 70 development area as an investment to fund early-stage development costs.

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6. Capital Assets (Continued)

	Balance July 1, 2017	Increases	Decreases	Balance June 30, 2018
Capital assets, not being depreciated/amortized:				
Land	\$ 105,582	\$ -	\$ 1,413	\$ 104,169
Construction in progress	13,655	25,850	13,294	26,211
Total capital assets, not being depreciated/ amortized	<u>119,237</u>	<u>25,850</u>	<u>14,707</u>	<u>130,380</u>
Capital assets, being depreciated/amortized:				
Facilities and improvements	582,568	7,891	-	590,459
Machinery and equipment	25,426	767	359	25,834
Intangible assets	2,264	-	-	2,264
Dredging	4,539	4,921	-	9,460
Waterfront Land Use Plan	2,779	16	-	2,795
Infrastructure	30,682	-	-	30,682
Total capital assets, being depreciated/ amortized	<u>648,258</u>	<u>13,595</u>	<u>359</u>	<u>661,494</u>
Less accumulated depreciation/amortization for:				
Facilities and improvements	302,598	12,528	-	315,126
Machinery and equipment	15,887	1,211	359	16,739
Intangible assets	2,198	36	-	2,234
Dredging	3,454	2,627	-	6,081
Waterfront Land Use Plan	2,739	56	-	2,795
Infrastructure	12,877	1,320	-	14,197
Total accumulated depreciation/amortization	<u>339,753</u>	<u>17,778</u>	<u>359</u>	<u>357,172</u>
Total capital assets, being depreciated/amortized, net	<u>308,505</u>	<u>(4,183)</u>	<u>-</u>	<u>304,322</u>
Capital assets, net	<u>\$ 427,742</u>	<u>\$ 21,667</u>	<u>\$ 14,707</u>	<u>\$ 434,702</u>

Facilities and improvements include pier substructures, which have an estimated useful life greater than 50 years. The cost of such long-lived assets totaled \$21,915,000 as of June 30, 2019 and 2018. Total interest expense was \$4,397,000 and \$4,479,000 for fiscal years 2019 and 2018, of which \$64,000 and \$18,000 was capitalized, respectively. Depreciation and amortization expense in 2018 included a negative \$4,732,000 adjustment derived from calculations using updated estimated useful lives for certain capital assets.

7. Other Noncurrent Assets

At June 30, 2019 and 2018, other noncurrent assets were \$2,731,000 and \$3,300,000. Other noncurrent assets represent the long-term portion of the lease or other agreement obligations from tenants and customers. In addition, the Port and a developer entered into a promissory note for \$1,500,000 to cover the cost of certain improvements that originated in fiscal year 2017 and unpaid as of June 30, 2019. Repayment is scheduled to commence at a future date following the Developer Equity Repayment Date which is the date that the outstanding developer equity is reduced to zero and the developer equity return is paid in full. Account balance includes interest receivable of \$135,000 on the principal balance disbursed and outstanding at the rate of 4.41% per annum, simple interest.

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8. Bonds, Loans and Other Payables

The changes in bonds, loans, and other payables for the years ended June 30, 2019 and 2018 are as follows (in thousands):

	July 1, 2018	Additional Obligations and Net Increases	Retirements and Net Decreases	June 30, 2019	Amounts Due Within One Year
Long-term debt:					
Revenue bonds	\$ 51,535	\$ -	\$ 1,390	\$ 50,145	\$ 1,455
Certificates of participation	31,170	-	1,160	30,010	1,215
Net of premiums/discounts:					
For issuance premiums	1,826	-	71	1,755	-
For issuance discounts	(192)	-	(9)	(183)	-
Total bonds payable	<u>84,339</u>	<u>-</u>	<u>2,612</u>	<u>81,727</u>	<u>2,670</u>
Other payables:					
Loan payables	1,976	6,144	143	7,977	409
Accrued vacation and sick leave pay	2,255	1,776	1,712	2,319	1,362
Accrued workers' compensation (Note 18)	3,000	159	611	2,548	417
Estimated claims payable (Note 18)	450	30	30	450	200
Pollution remediation obligations (Note 17)	3,044	1,105	-	4,149	44
Long-term obligations	<u>\$ 95,064</u>	<u>\$ 9,214</u>	<u>\$ 5,108</u>	<u>\$ 99,170</u>	<u>\$ 5,102</u>

	July 1, 2017	Additional Obligations and Net Increases	Retirements and Net Decreases	June 30, 2018	Amounts Due Within One Year
Long-term debt:					
Revenue bonds	\$ 52,860	\$ -	\$ 1,325	\$ 51,535	\$ 1,390
Certificates of participation	32,275	-	1,105	31,170	1,160
Net of premiums/discounts:					
For issuance premiums	1,898	-	72	1,826	-
For issuance discounts	(202)	-	(10)	(192)	-
Total bonds payable	<u>86,831</u>	<u>-</u>	<u>2,492</u>	<u>84,339</u>	<u>2,550</u>
Other payables:					
Loan payable	2,113	-	137	1,976	143
Accrued vacation and sick leave pay	2,167	1,688	1,600	2,255	1,346
Accrued workers' compensation (Note 18)	2,906	638	544	3,000	454
Estimated claims payable (Note 18)	1,125	-	675	450	200
Pollution remediation obligations (Note 17)	11,442	-	8,398	3,044	44
Long-term obligations	<u>\$ 106,584</u>	<u>\$ 2,326</u>	<u>\$ 13,846</u>	<u>\$ 95,064</u>	<u>\$ 4,737</u>

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8. Bonds, Loans and Other Payables (Continued)

Annual debt service requirements for all bonds and loans outstanding as of June 30, 2019 are as follows (in thousands):

<u>Fiscal Year Ending June 30</u>	<u>Revenue Bonds</u>		<u>Certificates of Participation</u>		<u>State Loan Payables</u>		<u>Total</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2020	\$ 1,455	\$ 2,718	\$ 1,215	\$ 1,516	\$ 409	\$ 358	\$ 3,079	\$ 4,592
2021	1,530	2,644	1,280	1,455	427	341	3,237	4,440
2022	1,625	2,550	1,340	1,391	446	322	3,411	4,263
2023	1,725	2,452	1,410	1,324	466	301	3,601	4,077
2024	1,830	2,341	740	1,253	487	281	3,057	3,875
2025-2029	11,125	9,744	4,300	5,666	2,786	1,052	18,211	16,462
2030-2034	10,770	6,131	5,545	4,420	2,205	475	18,520	11,026
2035-2039	12,425	3,487	7,110	2,849	751	46	20,286	6,382
2040-2044	7,660	840	7,070	906	-	-	14,730	1,746
Total	<u>\$ 50,145</u>	<u>\$ 32,907</u>	<u>\$ 30,010</u>	<u>\$ 20,780</u>	<u>\$ 7,977</u>	<u>\$ 3,176</u>	<u>\$ 88,132</u>	<u>\$ 56,863</u>
Remaining interest rates	<u>3.0% - 7.408%</u>		<u>4.75% - 5.25%</u>		<u>4.5%</u>			

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8. Bonds, Loans and Other Payables (Continued)

The Port Commission issued its Revenue Bonds under a Master Trust Indenture dated February 1, 2010 (Indenture), which provides for, among other things, the issuance of one or more series of bonds, the general terms and conditions of the bonds, and certain covenants made by the Port Commission for the benefit of the bondholders. The Revenue Bonds are special limited obligations of the Port Commission secured by and payable solely from the net revenues of the Port and are not an obligation of the City.

In May 2014, the Port issued \$22,675,000 in revenue bonds in two series; an AMT tax-exempt series (Series 2014A) and a taxable series (Series 2014B). Series 2014A included serial and term bonds totaling \$19,880,000 with coupon rates ranging from 3.00% to 5.00% and maturities from March 2020 to March 2044. Series 2014B included serial bonds totaling \$2,795,000 with coupon rates ranging from 0.55% to 3.00% and maturities from March 2015 through March 2020. Series 2014A bonds with scheduled maturities on or after March 2025 are subject to redemption as a whole or in part at the sole option of the Port at any time on or after March 2024 at redemption prices specified in the Indenture. Bonds with scheduled maturities on or before March 2024 are not subject to optional redemption prior to their maturity. Under the terms of the indenture, the Port is required to deposit in a debt service reserve fund with a bond trustee, amounts equal to the Series 2014A reserve requirement and the Series 2014B reserve requirement. The Series 2014A reserve requirement is an amount equal to the lesser of: a) the maximum annual debt service with respect to the Series 2014A bonds, b) 125% of the average annual debt service on the Series 2014A bonds, c) 10% of the initial principal amount of the Series 2014A bonds, or d) the sum of \$650,615, which is the initial deposit into the reserve fund, plus any amounts available to be transferred from the Series 2014B reserve account pursuant to the Indenture. Funds on deposit in the Series 2014A reserve fund are only for the benefit of the Series 2014A bondholders. The Series 2014B reserve requirement is an amount equal to the maximum annual debt service on the Series 2014B Bonds. Funds on deposit in the Series 2014B reserve fund are only for the benefit of the Series 2014B bondholders. At June 30, 2019, the Port was in compliance with the Series 2014A reserve requirement. In June 2019, a transfer from the Series 2014B reserve fund, to the interest debt service fund completed by the trustee bank based on its calculations, resulted in an insignificant shortfall versus the total required reserve account balance as of June 30, 2019. However, as of July 31, 2019, the balance in the reserve account met the required reserve.

In February 2010, the Port issued \$36,650,000 in revenue bonds in two series; a non-AMT tax-exempt series (Series 2010A) and a taxable series (Series 2010B). Series 2010A consists of a term bond totaling \$14,220,000 maturing March 2040 with a coupon rate of 5.125%. Series 2010B, original issue total of \$22,430,000, has serial and term bonds of \$15,645,000 outstanding at June 30, 2019 with remaining coupon rates ranging from 6.101% to 7.408% and remaining maturities from March 2020 through March 2030. Bonds with scheduled maturities on or after March 2021 are subject to redemption as a whole or in part at the sole option of the Port at any time on or after March 2020 at redemption prices specified in the Indenture. Bonds with scheduled maturities on or before March 2020 are not subject to optional redemption prior to their maturity. Under terms of the indenture, the Port is required to deposit in a debt service reserve fund with a bond trustee, an amount equal to the Series 2010A reserve requirement plus the Series 2010B reserve requirement. The Series 2010A reserve requirement is an amount equal to the lesser of: a) the maximum annual debt service with respect to the Series 2010A bonds, b) 125% of the average annual debt service on the Series 2010A bonds, c) 10% of the outstanding principal amount of the

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8. Bonds, Loans and Other Payables (Continued)

Series 2010A bonds, or d) \$728,775, which is the initial deposit into the reserve fund. Funds on deposit in the Series 2010A reserve fund are only for the benefit of the Series 2010A bondholders. At June 30, 2019, the Port was in compliance with the Series 2010A reserve requirement.

The Series 2010B reserve requirement is an amount equal to the maximum annual debt service on the Series 2010B Bonds. Funds on deposit in the Series 2010B reserve fund are only for the benefit of the Series 2010B bondholders. In June 2019, a transfer from the Series 2010B reserve fund, to the interest debt service fund completed by the trustee bank based on its calculations, resulted in an insignificant shortfall versus the total required reserve account balance as of June 30, 2019. Shortly after, in July 2019, additional funds were posted to the reserve account to ensure the reserve requirement was met.

The Port has pledged future net revenues to repay the Revenue Bonds. Annual principal and interest payments through 2044 are expected to require less than 11% of net pledged revenues as calculated in accordance with the bond indenture. The total principal and interest remaining to be paid on the bonds is \$83,052,000. The principal and interest payments made in 2019 were \$4,176,000 and pledged revenues (total net revenues calculated in accordance with the bond Indenture) were \$38,913,000. The principal and interest payments made in 2018 were \$4,174,000 and pledged revenues (total net revenues calculated in accordance with the bond Indenture) were \$36,197,000.

While revenue bonds are outstanding, the Port may not create liens on its property essential to its operations or dispose of any property essential to maintaining operating activity at a level necessary for it to meet its covenants, including its covenant to maintain net revenue coverage. The Port also is required to maintain specified insurance or qualified self-insurance. The Port is not required to carry earthquake insurance. Covenants of the Indenture include that the Port will manage its business operations, establish and maintain rentals, fees and charges for the use of Port property and for services provided by the Port so that the net revenue, as defined in the Indenture, in each fiscal year will be at least equal to 130% of aggregate annual debt service for such fiscal year. At June 30, 2019, the Port was in compliance with such bond covenants.

The revenue bonds contain an acceleration provision that in an event of default, the trustee may, upon written request from the credit provider or holders of not less than fifty-one percent of the aggregate principal amount then outstanding, by written notice to the Commission, shall declare the principal amount of all bonds outstanding and the interest accrued becomes due and payable immediately.

The revenue bonds are subject to an arbitrage rebate requirement. Under U.S. Treasury Department regulations, all government tax-exempt debt issued after August 21, 1986 is subject to arbitrage rebate requirements. The requirements stipulate, in general, that earnings from the investment of tax-exempt bond proceeds that exceed related interest costs on the bonds must be remitted to the federal government on the fifth anniversary of each bond issue. There was no cumulative arbitrage liability with respect to the revenue bonds as of June 30, 2019 and 2018.

In May 2012, the Board of Supervisors authorized the City to issue \$45 million in certificates of participation (COPs) to finance various facilities and improvements under the jurisdiction of the Port, including the construction of a primary cruise terminal at Pier 27. The public sale of

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8. Bonds, Loans and Other Payables (Continued)

\$37,700,000 in COPs was completed in October 2013. The COPs were issued in two series, consisting of Series 2013B (Non-AMT) in the amount of \$4,830,000 and Series 2013C (AMT) in the amount of \$32,870,000. Series 2013B certificates will mature March 2036 and March 2038, and carry coupon rates of 5.25% and 4.75%, respectively. Series 2013C certificates mature March 2014 through March 2043 and carry coupon rates between 4.00% and 5.25%. The COPs with scheduled maturities on or after March 2023 are subject to redemption at specified prices at the option of the City. Those COPs with scheduled maturities before March 2023 are not subject to optional redemption prior to their maturity.

A memorandum of understanding between the City and the Port governs the terms of repayment for the City COPs. The Port is required to make payments to the City equal to annual debt service on the COPs. These payment obligations are subordinate to any Port revenue bond obligations. The Port has agreed, during the term of the COPs, to annually budget amounts necessary for direct payment of obligations or for reimbursement by the Port to the City for costs incurred on behalf of the Port in connection with the COPs. While the completed cruise terminal serves as the leased asset for the COPs to secure the City's covenants and obligations under the lease, there is no remedy under the COPs for the purchasers thereof to take possession of the leased property. In an event of default, the trustee may enforce all of its rights and remedies under the project lease, including the right to recover base rental payments as they become due under the project lease by pursuing any remedy available in law or in equity, other than by terminating the project lease or re-entering and reletting the leased property, or except as expressly provided in the project lease.

The Port has entered into a loan agreement with the California Division of Boating and Waterways (Cal Boating) for \$3,500,000 to finance certain Hyde Street Harbor improvements. The loan is subordinate to all bonds payable by the Port and interest accrues at a rate of 4.5% per annum on the unpaid balance over 30 years. The project was completed in 2002, and annual payments commenced on August 1, 2002. The loan is secured by gross revenues as defined in the loan agreement. Total principal and interest remaining to be paid on this loan are \$2,317,000. Annual principal and interest payments were \$232,000 in 2019 and 2018 and pledged harbor revenues were \$157,000 and \$95,000 for the years ended June 30, 2019 and 2018, respectively. The loan contains a provision that in an event the Port fails, in whole or in part, to make any payment due under Fisherman's Wharf loan contract, then such a deficiency shall be added to and become part of the principal of the loan and a provision that if any annual loan installment payment made by the Port is less than the amount required under the terms of the contract, then such payment shall first be applied to reduce any accrued unpaid interest due on the loan while any remaining part of the payment shall be used to reduce the principal of the loan.

Effective May 1, 2019, the Port assumed the operations and corresponding balances of the South Beach Harbor from the Office of Community Investment and Infrastructure, including three loans provided by Cal Boating, which totaled \$6,144,000 and accrues interest at a rate of 4.5% per annum. Total principal and interest remaining to be paid on the loans are \$8,836,000. These loans are secured by net revenues as defined in the loan agreements. Annual principal and interest payments were \$536,000 in 2019 and pledged net revenues were \$2,059,000 for the year ended June 30, 2019. Cal Boating may take possession of the operations if after ninety days written notice, the Port remains in breach of any of the provisions of Small Craft Harbor loans and operation contract. Cal Boating shall operate or maintain the operations for the account of the Port until the loan is repaid in full.

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8. Bonds, Loans and Other Payables (Continued)

Also, in conjunction with the receipt of SBH, the Port designated SBH as a Special Facility and the Cal Boating Loans as Special Facility Bonds as provided under the Port’s Revenue Bond Master Trust Indenture. Pursuant to Section 2.14 of the Revenue Bond Master Trust Indenture, the Commission is authorized to designate an existing or planned facility, structure, equipment or other property, real or personal property that is located within the Port Area as a Special Facility. The Commission may designate revenue earned by the Port from or with respect to a Special Facility as “Special Facility Revenue”. Special Facility Revenue is not included in revenue as defined in the Revenue Bond Master Trust Indenture, and, consequently, is not included in the Net Revenues that is pledged as security for the Revenue Bonds under the Revenue Bond Master Trust Indenture.

Segment information

The Port fund and the South Beach Harbor fund are reported in a single enterprise in fiscal year 2019. Summary financial information with individual activities for the Port enterprise is presented below:

Condensed statements of net position (in thousands)

	June 30, 2019		
	Port (excluding SBH)	South Beach Harbor (SBH)	Port Enterprise Total
Assets:			
Current and other assets	\$ 222,575	\$ 5,244	\$ 227,819
Capital assets	444,262	20,010	464,272
Total assets	<u>666,837</u>	<u>25,254</u>	<u>692,091</u>
Deferred outflows of resources	<u>14,547</u>	<u>-</u>	<u>14,547</u>
Liabilities:			
Current liabilities	30,822	1,103	31,925
Noncurrent liabilities	228,282	5,884	234,166
Total liabilities	<u>259,104</u>	<u>6,987</u>	<u>266,091</u>
Deferred inflows of resources	<u>9,909</u>	<u>-</u>	<u>9,909</u>
Net position:			
Net investment in capital assets	320,645	13,543	334,188
Restricted	14,467	-	14,467
Unrestricted	77,259	4,724	81,983
Total net position	<u>\$ 412,371</u>	<u>\$ 18,267</u>	<u>\$ 430,638</u>

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8. Bonds, Loans and Other Payables (Continued)

**Condensed statements of revenues, expenses,
and changes in fund net position (in thousands)**

	Year Ended June 30, 2019		
	Port (excluding SBH)	South Beach Harbor (SBH)	Port Enterprise Total
Revenues:			
Operating revenues	\$ 121,162	\$ 871	\$ 122,033
Nonoperating revenues	9,520	18,340	27,860
Capital contributions	1,909	-	1,909
Total revenues	<u>132,591</u>	<u>19,211</u>	<u>151,802</u>
Expenses:			
Operating expenses	111,356 **	752	112,108
Nonoperating expenses	10,962	46	11,008
Total expenses	<u>122,318</u>	<u>798</u>	<u>123,116</u>
Change in net position	10,273	18,413	28,686
Net position, beginning of year	402,098	(146) *	401,952
Net position, end of the year	<u>\$ 412,371</u>	<u>\$ 18,267</u>	<u>\$ 430,638</u>

* Beginning net position of South Beach Harbor of (\$146,000) is primarily related to accumulated capital expenditures funded by SBH operations.

** Includes SBH pension and OPEB expenses.

Condensed statements of cash flows (in thousands)

	Year Ended June 30, 2019		
	Port (excluding SBH)	South Beach Harbor (SBH)	Port Enterprise Total
Net cash provided by (used in):			
Operating activities	\$ 30,181	\$ 224	\$ 30,405
Noncapital financing activities	(5,952)	5,078	(874)
Capital and related financing activities	(38,465)	(186)	(38,651)
Investing activities	5,465	-	5,465
Increase/(decrease) in cash and cash equivalents	(8,771)	5,116	(3,655)
Cash and cash equivalents at beginning of year	196,388	28	196,416
Cash and cash equivalents at end of year	<u>\$ 187,617</u>	<u>\$ 5,144</u>	<u>\$ 192,761</u>

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9. Operating Revenues – Property Rentals

Certain property rental agreements specify rental payments based on a percentage of tenant sales, subject to a minimum amount. For the years ended June 30, 2019 and 2018, property rental revenues were comprised as follows (in thousands):

	2019	2018
Minimum rentals, all revenue types	\$ 68,787	\$ 65,321
Percentage rentals	16,712	16,773
Total	\$ 85,499	\$ 82,094

The future minimum rent revenues under noncancelable operating leases having terms in excess of one year as of June 30, 2019 are as follows (in thousands):

Year Ending June 30	
2020	\$ 47,323
2021	42,890
2022	38,800
2023	32,526
2024	25,021
2025-2029	96,800
2030-2034	82,421
2035-2039	64,160
2040-2044	43,010
2045-2049	37,159
2050-2054	16,289
2055-2059	14,575
2060-2064	14,519
2065-2069	10,764
2070-2074	5,242
2075-2077	2,456
Total	\$ 573,955

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9. Operating Revenues – Property Rentals (Continued)

In October 2018, the Port received participation income of \$10,300,000 from the sale and transfer of the Ferry Building master lease. The developer entered into a 66-year ground lease, expiring in 2067, with the Port. Future revenues for this lease are included above.

Property subject to operating leases and property held for lease at June 30, 2019 and 2018 consisted of the following (in thousands):

	<u>2019</u>	<u>2018</u>
Land	\$ 60,130	\$ 51,800
Facilities and improvements at cost, net of accumulated depreciation	<u>140,841</u>	<u>123,854</u>
Total	<u>\$ 200,971</u>	<u>\$ 175,654</u>

Under the terms of some long-term leases, certain minimum rent obligations are fulfilled by the completion of major tenant-financed rehabilitation and improvement work that benefits the Port. The Port records these improvements and the related obligation for tenant improvement credits upon the certified completion and acceptance of the agreed work.

10. Retirement Plan

The City participates in a cost-sharing multiple-employer defined benefit pension plan (the Plan). The Plan is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, pension expense, information about the fiduciary net position of the Plan, and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by the Retirement System. Benefit payments (including refunds of employee contributions) are recognized when currently due and payable in accordance with the benefit terms. Investments are reported at fair value.

GASB 68 requires that the reported results must pertain to liability and asset information within certain defined timeframes. For this report, the following timeframes are used.

	<u>2019</u>	<u>2018</u>
Valuation Date	June 30, 2017 updated to June 30, 2018	June 30, 2016 updated to June 30, 2017
Measurement Date	June 30, 2018	June 30, 2017
Measurement Period	July 1, 2017 to June 30, 2018	July 1, 2016 to June 30, 2017

The City is an employer of the Plan with a proportionate share of 94.10% as of the June 30, 2018 measurement date and 94.07% as of the June 30, 2017 measurement date. The Port's allocation percentage was determined based on the Port's employer contributions divided by the City's total employer contributions for each measurement period. The Port's net pension liability, deferred outflows/inflows of resources related to pensions, amortization of deferred outflows/inflows and pension expense are based on the Port's allocated percentage. The Port's allocation of the City's

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10. Retirement Plan (Continued)

proportionate share was approximately 0.94% as of the June 30, 2018 measurement date and 0.93% as of the June 30, 2017 measurement date.

Plan Description - The Plan provides basic service retirement, disability, and death benefits based on specified percentages of defined final average monthly salary and provides annual cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and the Administrative Code are the authorities which establish and amend the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained on the Retirement System's website <http://mysfers.org> or by writing to the San Francisco Employees' Retirement System, 1145 Market Street, 5th Floor, San Francisco, CA 94103 or by calling (415) 487-7000.

Benefits - The Retirement System provides service retirement, disability and death benefits based on specified percentages of defined final average monthly salary and annual cost of living adjustments (COLA) after retirement. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan. The Retirement System pays benefits according to the category of employment and the type of benefit coverage provided by the City and County. The four main categories of Plan members are:

- Miscellaneous Non-Safety Members – staff, operational, supervisory, and all other eligible employees who are not in special membership categories.
- Sheriff's Department and Miscellaneous Safety Members – sheriffs assuming office on and after January 7, 2012, and undersheriffs, deputized personnel of the sheriff's department, and miscellaneous safety employees hired on and after January 7, 2012.
- Firefighter Members – firefighters and other employees whose principal duties are in fire prevention and suppression work or who occupy positions designated by law as firefighter member positions.
- Police Members – police officers and other employees whose principal duties are in active law enforcement or who occupy positions designated by law as police member positions.

The membership groups and the related service retirement benefits are included in the Notes to the Basic Financial Statements of San Francisco Employees' Retirement System.

All members are eligible to apply for a disability retirement benefit, regardless of age, when they have 10 or more years of credited service and they sustain an injury or illness that prevents them from performing their duties. Safety members are eligible to apply for an industrial disability retirement benefit from their first day on the job if their disability is caused by an illness or injury that they receive while performing their duties.

All retired members receive a benefit adjustment each July 1, which is the Basic COLA. The majority of adjustments are determined by changes in CPI with increases capped at 2%. The Plan

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10. Retirement Plan (Continued)

provides for a Supplemental COLA in years when there are sufficient “excess” investment earnings in the Plan. The maximum benefit adjustment each July 1 is 3.5% including the Basic COLA. Effective July 1, 2012, voters approved changes in the criteria for payment of the Supplemental COLA benefit, so that Supplemental COLAs would only be paid when the Plan is also fully funded on a market value of assets basis (Proposition C). Certain provisions of this voter-approved proposition were challenged in the Courts. A decision by the California Courts modified the interpretation of the proposition. Effective July 1, 2012, members who retired before November 6, 1996 will receive a Supplemental COLA only when the Plan is also fully funded on a market value of assets basis. However, the “full funding” requirement does not apply to members who retired on or after November 6, 1996 and were hired before January 7, 2012. For all members hired before January 7, 2012, all Supplemental COLAs paid to them in retirement benefits will continue into the future even where an additional Supplemental COLA is not payable in any given year. For members hired on and after January 7, 2012, a Supplemental COLA will only be paid to retirees when the Plan is fully funded on a market value of assets basis and in addition for these members, Supplemental COLAs will not be permanent adjustments to retirement benefits. That is, in years when a Supplemental COLA is not paid, all previously paid Supplemental COLAs will expire.

Funding and Contribution Policy – Contributions are made to the basic plan by both the City and participating employees. Employee contributions are mandatory as required by the Charter. Employee contribution rates for fiscal year 2019 and 2018 varied from 7.5% to 13.0% as a percentage of gross covered salary. Most employee groups agreed through collective bargaining for employees to contribute the full amount of the employee contributions on a pretax basis. The City is required to contribute at an actuarially determined rate. Based on the July 1, 2017 actuarial report, the required employer contribution rate for fiscal year 2019 was 18.81% to 23.31% and based on the July 1, 2016 actuarial report, the required employer contribution rate for fiscal year 2018 was 18.96% to 23.46%.

Employer contributions and employee contributions made by the employer to the Plan are recognized when due and the employer has made a formal commitment to provide the contributions. The City’s proportionate share of employer contributions recognized by the Retirement System in fiscal years ended June 30, 2018 and 2017 (measurement years) were \$582.6 million and \$519.1 million, respectively. The Port’s allocation of employer contributions for the 2018 measurement period was \$5,424,000 and for the 2017 measurement period was \$4,891,000.

Pension Liabilities, Pension Expenses and Deferred Outflows/Inflows of Resources Related to Pensions – As of June 30, 2019, the City reported a net pension liability for its proportionate share of the net pension liability of the Plan of \$4.03 billion. The City’s net pension liability for the Plan is measured as the proportionate share of the net pension liability. The net pension liability of the Plan is measured as of June 30, 2018 (measurement date), and the total pension liability for the Plan used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2017 rolled forward to June 30, 2018 using standard update procedures. The City’s proportion of the net pension liability was based on a projection of the City’s long-term share of contributions to the pension plan relative to the projected contributions of all participating employers, actuarially determined. The Port’s allocation of the City’s proportionate share of the net pension liability for Plan as of June 30, 2019 and 2018 (reporting years) were \$38,027,000 and

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10. Retirement Plan (Continued)

\$43,730,000, respectively. During the measurement year 2017-18, contributions and investment income decreased the net pension liability, which was partially offset by service costs and interest costs. During the measurement year 2016-17, the actual investment earnings decreased the net pension liability. This was only partially offset by an increase in service costs and interest costs, resulting in an overall decrease in the net pension liability reported at June 30, 2018.

For the years ended June 30, 2019 and 2018, the City's recognized pension expense, including amortization of deferred outflows/inflows related pension items, were \$0.49 billion and \$0.73 billion, respectively. The Port's allocation of pension expense, including amortization of deferred outflows/inflows related pension items for 2019 and 2018, were \$5,064,000 and \$6,417,000, respectively. Pension expense decreased in 2019 and 2018, largely due to the impact of actual investment earnings.

At June 30, 2019, the Port reported deferred outflows of resources and deferred inflows of resources related to pension were the following (in thousands):

	June 30, 2019	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Pension contributions subsequent to measurement date	\$ 5,731	\$ -
Differences between expected and actual experience	309	1,076
Change in assumptions	5,929	-
Net difference between projected and actual earnings on pension plan investments	-	6,112
Change in proportionate share	54	36
	\$ 12,023	\$ 7,224

At June 30, 2018, the Port reported deferred outflows of resources and deferred inflows of resources related to pension were the following (in thousands):

	June 30, 2018	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Pension contributions subsequent to measurement date	\$ 5,424	\$ -
Differences between expected and actual experience	406	1,320
Change in assumptions	7,091	128
Net difference between projected and actual earnings on pension plan investments	-	1,631
Change in proportionate share	65	72
	\$ 12,986	\$ 3,151

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10. Retirement Plan (Continued)

The pension contributions made subsequent to the measurement date will be applied to the net pension liability in the next period. All other deferred outflows and deferred inflows of resources will be amortized annually and recognized as pension expense as follows (in thousands):

Year Ending	Deferred Outflows
June 30	(Inflows) of Resources
2020	\$ 2,427
2021	1,067
2022	(3,126)
2023	(1,300)

Actuarial Assumptions – A summary of the actuarial assumptions and methods used to calculate the total pension liability as of measurement dates June 30, 2018 and 2017 (measurement years) is provided below. Refer to the July 1, 2017 and 2016 actuarial valuation reports for a complete description of all other assumptions, which can be found on the Retirement System’s website <http://mysfers.org>.

	2019	2018
Valuation Date	June 30, 2017 updated to June 30, 2018	June 30, 2016 updated to June 30, 2017
Measurement Date	June 30, 2018	June 30, 2017
Actuarial Cost Method	Entry-Age Normal Cost	Entry-Age Normal Cost
Expected Rate of Return	7.5%	7.5%
Municipal Bond Yield	3.87% as of June 30, 2018	3.58% as of June 30, 2017
	Bond Buyer 20-Bond-GO Bond Index	Bond Buyer 20-Bond-GO Bond Index
	June 28, 2018	June 29, 2017
Discount Rate	7.50% as of June 30, 2018	7.50% as of June 30, 2017
Administrative Expenses	0.60% of payroll as of June 30, 2018	0.60% of payroll as of June 30, 2017
Basic COLA	<u>June 30, 2018</u>	<u>June 30, 2017</u>
Old Miscellaneous and all New Plans	2.00%	2.00%
Old Police & Fire pre 7/1/75 Retirements	2.50%	2.70%
Old Police & Fire, Charters A8.595 & A8.596	3.10%	3.30%
Old Police & Fire, Charters A8.559 & A8.585	4.20%	4.40%

Mortality rates for active members and healthy annuitants were based upon the adjusted Employee and Healthy Annuitant CALPERS mortality tables projected generationally from the 2009 base year using a modified version of the MP-2015 projection scale.

Discount Rate – The beginning and end of year measurements are based on different assumptions and contribution methods that may result in different discount rates. The discount rate used to measure the total pension liability as of June 30, 2018 and 2017 (measurement dates) was 7.50%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will continue to be made at the rates specified in the Charter. Employer contributions were assumed to be made in accordance with the contribution policy in effect for July 1, 2017 and 2016 actuarial valuations. That policy includes contributions equal to the employer portion of the Entry Age normal costs for members as of the valuation date, a payment for the expected administrative expenses, and an amortization payment on the unfunded actuarial liability.

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10. Retirement Plan (Continued)

The amortization payment is based on closed periods that vary in length depending on the source. Charter amendments prior to July 1, 2014 are amortized over 20 years. After July 1, 2014, any Charter changes to active member benefits are amortized over 15 years and changes to inactive member benefits, including Supplemental COLAs, are amortized over 5 years. The remaining Unfunded Actuarial Liability not attributable to Charter amendments as of July 1, 2013 is amortized over a 19-year period commencing July 1, 2014. Experience gains and losses and assumption or method changes on or after July 1, 2014 are amortized over 20 years. For the July 1, 2016 valuation, the increase in the Unfunded Actuarial Liability attributable to the Supplemental COLAs granted on July 1, 2013 and July 1, 2014 are amortized over 17 years and 5 years respectively. All amortization schedules are established as a level percentage of payroll, so payments increase 3.50% each year. The Unfunded Actuarial Liability is based on an Actuarial Value of Assets that smooths investment gains and losses over five years and a measurement of the Actuarial Liability that excludes the value of any future Supplemental COLAs.

While the contributions and measure of Actuarial Liability in the valuation do not anticipate any future Supplemental COLAs, the projected contributions for the determination of the discount rate include the anticipated future amortization payments on future Supplemental COLAs for current members when they are expected to be granted. For members who worked after November 6, 1996 and before Proposition C passed, a Supplemental COLA is granted if the actual investment earnings during the year exceed the expected investment earnings on the Actuarial Value of Assets. For members who did not work after November 6, 1996 and before Proposition C passed, the Market Value of Assets must also exceed the actuarial liability at the beginning of the year for a Supplemental COLA to be granted. When a Supplemental COLA is granted, the amount depends on the amount of excess earnings and the basic COLA amount for each membership group. The large majority of members receive a 1.50% Supplemental COLA when granted.

Because the probability of a Supplemental COLA depends on the current funded level of the System for certain members, the following assumptions were developed for the probability and amount of Supplemental COLA for each future year. The City has assumed that a full Supplemental COLA will be paid to all post-1996 retirees effective July 1, 2018. The table below shows the net assumed Supplemental COLA for members with a 2.00% Basic COLA for sample years.

**Assumed Supplemental COLA for Members
with a 2.00% Basic COLA**

	<u>June 30, 2018 Valuation</u>			<u>June 30, 2017 Valuation</u>	
	<u>1996 - Prop C</u>	<u>Before 11/06/96 or after Prop C</u>		<u>1996 - Prop C</u>	<u>Before 11/06/96 or after Prop C</u>
2019	0.75%	0.00%	2018	0.75%	0.00%
2022	0.75%	0.29%	2023	0.75%	0.29%
2025	0.75%	0.35%	2028	0.75%	0.35%
2028	0.75%	0.36%	2033	0.75%	0.38%
2031 and thereafter	0.75%	0.38%	2038 and thereafter	0.75%	0.38%

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10. Retirement Plan (Continued)

The projection of benefit payments to current members for determining the discount rate includes the payment of anticipated future Supplemental COLAs.

Based on these assumptions, the Retirement System’s fiduciary net position was projected to be available to make projected future benefit payments for current members until fiscal year end 2097 when only a portion of the projected benefit payments can be made from the projected fiduciary net position. Projected benefit payments are discounted at the long-term expected return on assets of 7.50% to the extent the fiduciary net position is available to make the payments and at the municipal bond rate of 3.87% to the extent they are not available. The single equivalent rate used to determine the total pension liability as of June 30, 2018 is 7.50%.

The long-term expected rate of return on pension plan investments was 7.50%. It was set by the Retirement Board after consideration of both expected future returns and historical returns experienced by the Retirement System. Expected future returns were determined by using a building-block method in which best-estimate ranges of expected future real rates of return were developed for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Target allocation and best estimates of geometric long-term expected real rates of return (net of pension plan investment expense and inflation) for each major asset class are summarized in the following table.

Long-Term Expected Real Rates of Return

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Global Equity	31.0%	5.4%
Treasuries	6.0%	0.5%
Liquid Credit	3.0%	3.3%
Private Credit	10.0%	4.6%
Private Equity	18.0%	6.6%
Real Assets	17.0%	4.5%
Hedge Funds/Absolute Returns	15.0%	3.7%

Sensitivity of Proportionate Share of the Net Pension Liability (NPL) to Changes in the Discount Rate – The following presents the Port’s allocation of the employer’s proportionate share of the net pension liability for the Plan, calculated using the discount rate, as well as what the Port’s allocation of the employer’s proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1% lower or 1% higher than the current rate.

<u>Measurement Year</u>	<u>(\$000's)</u>		
	<u>1% Decrease Share of NPL @ 6.50%</u>	<u>Allocated Share of NPL @ 7.50%</u>	<u>1% Increase Share of NPL @ 8.50%</u>
June 30, 2018	\$ 71,221	\$ 38,027	\$ 10,579
June 30, 2017	74,916	43,730	17,925

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11. Health Service System

Health care benefits for Port employees, retired employees, and surviving spouses are financed by beneficiaries and by the City principally through the City and County of San Francisco Health Service System. The annual contribution to the City health plan is determined by Charter provision based on similar contributions made by the ten most populous counties in California.

The City Health Service System issues a publicly available financial report that includes financial statements and required supplementary information for the health care benefits. That report can be found on its website <http://www.myhss.org> or may be obtained by writing to the San Francisco Health Service System, 1145 Market Street, Suite 200, San Francisco, CA 94103 or by calling (800) 541-2266.

12. Other Postemployment Benefits (OPEB)

Plan Descriptions – Port participates in a single-employer defined benefit other postemployment benefits plan (the OPEB Plan), which is administered through the City’s Health Service System in the Retiree Health Care Trust Fund (Trust Fund). It provides postemployment medical, dental and vision insurance benefits to eligible employees, retired employees, surviving spouses, and domestic partners. Health benefit provisions are established and may be amended through negotiations between the City and the respective bargaining units. The City does not issue a separate report on its other postemployment benefit plan.

GASB 75 requires that reported results must pertain to liability and asset information within certain defined timeframes. For this report, the following timeframes are used.

San Francisco Health Service System Retiree Plan

Valuation Date	June 30, 2018
Measurement Date	June 30, 2018
Measurement Period	July 1, 2017 and June 30, 2018

The Port’s proportionate share percentage of the OPEB Plan was determined based on its percentage of citywide “pay-as-you-go” contributions for the year ended June 30, 2018. The Port’s net OPEB liability, deferred outflows/inflows of resources related to OPEB, amortization of deferred outflows/inflows and OPEB expense to each department is based on the Port’s allocated percentage. The Port’s proportionate share of the City’s OPEB elements were 0.80% as of June 30, 2018 measurement date and 0.83% as of June 30, 2017 measurement date.

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12. Other Postemployment Benefits (OPEB) (Continued)

Benefits – Permanent full-time and elected employees are eligible to retire and receive postretirement health insurance benefits when they are eligible for retirement benefits from the City and County of San Francisco’s Retirement System. The eligibility requirements are as follows:

Normal Retirement	Miscellaneous	Age 50 with 20 years of credited service ¹ Age 60 with 10 years of credited service
	Safety	Age 50 with 5 years of credited service
Disabled Retirement ²		Any age with 10 years of credited service
Terminated Vested ³		5 years of credited service at separation

¹ Age 53 with 20 years of credited service, age 60 with 10 years of credited service, or age 65 for Miscellaneous members hired on or after January 7, 2012.

² No service requirement for Safety members retiring under the industrial disability benefit or for surviving spouses / domestic partners of those killed in the line of duty.

³ Effective with Proposition B, passed on June 3, 2008, participants hired on or after January 10, 2009 must retire within 180 days of separation in order to be eligible for retiree healthcare benefits.

Retiree healthcare benefits are administered by the San Francisco Health Service System and include the following:

Medical:	PPO - City Health Plan (Self-insured) HMO - Kaiser (fully-insured) and Blue Shield (flex-funded)
Dental:	Delta Dental and DeltaCare USA
Vision:	Vision benefits are provided under the medical insurance plans and are administered by Vision Service Plan

Projections of the sharing of benefit related costs are based on an established pattern of practice.

Contributions – Benefits provided under the OPEB Plan are currently paid through “pay-as-you-go” funding. Additionally, under the City Charter, active officers and employees of the City who commenced employment on or after January 10, 2009, shall contribute to the Trust Fund a percentage of compensation not to exceed 2% of pre-tax compensation. The City shall contribute 1% of compensation for officers and employees who commenced employment on or after January 10, 2009 until the City’s GASB Actuary has determined that the City’s portion of the Trust Fund is fully funded. At that time, the City’s 1% contribution shall cease, and officers and employees will each contribute 50% of the maximum 2% of pre-tax compensation.

Starting July 1, 2016, active officers and employees of the City who commenced employment on or before January 9, 2009, shall contribute 0.25% of pre-tax compensation into the Trust Fund. Beginning on July 1st of each subsequent year, the active officers and employees of the City who commenced employment on or before January 9, 2009, shall contribute an additional 0.25% of pre-tax compensation up to a maximum of 1%. Starting July 1, 2016, the City shall contribute 0.25% of compensation into the Trust Fund for each officer and employee who commenced employment

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12. Other Postemployment Benefits (OPEB) (Continued)

on or before January 9, 2009. Beginning on July 1st of each subsequent year, the City shall contribute an additional 0.25% of compensation, up to a maximum of 1% for each officer and employee who commenced employment on or before January 9, 2009. When the City’s actuary has determined that the City’s portion of the Trust Fund is fully funded, the City’s 1% contribution shall cease, and officers and employees will each contribute 50% of the maximum 1% of pre-tax compensation.

Additional or existing contribution requirements may be established or modified by amendment to the City’s Charter.

For the years ended June 30, 2019 and 2018, the City’s funding was based on “pay-as-you-go” plus a contribution of \$32,786,000 and \$25,839,000 to the Trust Fund. The “pay-as-you-go” portions paid by the City were \$185,839,000 for a total contribution of \$218,625,000 for the year ended June 30, 2019 and \$178,019,000 for a total contribution of \$203,858,000 for the year ended June 30, 2018. The Port’s proportionate share of the City’s contributions for fiscal years 2019 and 2018 were \$1,758,000 and \$1,686,000, respectively.

OPEB Liabilities, OPEB Expenses and Deferred Outflows/Inflows of Resources Related to OPEB – As of June 30, 2019 and 2018, the City reported net OPEB liabilities related to the OPEB Plan of \$3.6 billion and \$3.7 billion, respectively. The Port’s proportionate share of the City’s net OPEB liability as of June 30, 2019 and 2018 were \$28,956,000 and \$30,750,000, respectively.

For the year ended June 30, 2019, the City’s recognized OPEB expense in the amount of \$320.3 million. Amortization of the City’s deferred outflows and inflows is included as a component of OPEB expense. The Port’s proportionate share of the City’s OPEB expense was \$1,762,000. For the year ended June 30, 2018, the City’s recognized OPEB expense in the amount of \$355.2 million and the Port’s proportionate share of the City’s OPEB expense was \$2,938,000.

As of June 30, 2019, the Port reported its proportionate share of the City’s deferred outflows/inflows of resources related to OPEB from the following sources (in thousands):

	June 30, 2019	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Contributions subsequent to measurement date	\$ 1,758	\$ -
Difference between expected and actual experience	-	2,658
Changes in assumptions	766	
Net difference between projected and actual earnings on plan investments	-	27
Total	\$ 2,524	\$ 2,685

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12. Other Postemployment Benefits (OPEB) (Continued)

As of June 30, 2018, the Port reported its proportionate share of the City's deferred outflows/inflows of resources related to OPEB from the following sources (in thousands):

	June 30, 2018	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Contributions subsequent to measurement date	\$ 1,686	\$ -
Net difference between projected and actual earnings on plan investments	-	50
Total	\$ 1,686	\$ 50

Amounts reported as deferred outflows, exclusive of contributions made after the measurement date, and deferred inflows of resources will be amortized annually and recognized in OPEB expense as follows (in thousands):

Year ended June 30	Deferred Inflows of Resources
2020	\$ (325)
2021	(325)
2022	(325)
2023	(315)
2024	(315)
Thereafter	(314)

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12. Other Postemployment Benefits (OPEB) (Continued)

Actuarial Assumptions – A summary of the actuarial assumptions and methods used to calculate the total OPEB liability as of June 30, 2018 (measurement date) is provided below:

Valuation Date	June 30, 2018
Measurement Date	June 30, 2018
Actuarial Cost Method	The Entry Age Actuarial Cost Method is used to measure the Plan's Total OPEB Liability
Healthcare Cost Trend Rates	Pre-Medicare trend starts at 6.50% and trends down to ultimate rate of 3.93% in 2076 Medicare trend starts at 7.50% and trends down to ultimate rate of 3.93% in 2076 10-County average trend starts at 5.90% and trends down to ultimate rate of 3.93% in 2076 Vision and expenses trend remains a flat 3.50% for all years
Expected Rate of Return on Plan Assets	7.40%
Discount Rate	7.40%
Salary Increase Rate	Wage Inflation Component: 3.50% Additional Merit Component (dependent on years of service): Police: 1.50% - 8.00% Fire: 1.50% - 15.00% Muni Drivers: 0.00% - 15.00% Craft: 0.00% - 3.50% Misc: 0.00% - 5.25%
Inflation Rate	Wage Inflation: 3.50% compounded annually Consumer Price Inflation: 2.75% compounded annually
Mortality Tables	Base mortality tables are developed by multiplying a published table by an adjustment factor developed in Retirement System experience study for the period ended June 30, 2014. Non-Annuitant - CalPERS employee mortality tables without scale BB projection

Adjustment		
Gender	Factor	Base Year
Female	0.918	2009
Male	0.948	2009

Healthy Annuitants - CalPERS healthy annuitant mortality table without scale BB projection

Adjustment		
Gender	Factor	Base Year
Female	1.014	2009
Male	0.909	2009

Miscellaneous Disabled Annuitants - RP-2014 Disabled Retiree Tables without MP-2014 projection

Adjustment		
Gender	Factor	Base Year
Female	1.066	2006
Male	0.942	2006

Safety Disabled Annuitants - CalPERS industrial disability mortality table without scale BB projection

Adjustment		
Gender	Factor	Base Year
Female	0.983	2009
Male	0.909	2009

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12. Other Postemployment Benefits (OPEB) (Continued)

The mortality rates in the base tables are projected generationally from the base year using the modified version of the MP-2015 projection scale. The scale was modified using the Society of Actuaries' model implementation tool with rates converging to the ultimate rate in 2017 (instead of 2029) and an ultimate rate of improvement of 0.85% (instead of 1.00%) up to age 85 decreasing to 0.70% (instead of 0.85%) at age 95.

Sensitivity of Liabilities to Changes in the Healthcare Cost Trend Rate and Discount Rate – The following presents the Port's proportionate share of the City's net OPEB liability calculated using the healthcare cost trend rate, as well as what the Port's allocation of the City's net OPEB liability would be if it were calculated using a healthcare cost trend rate that is 1% lower or 1% higher than the current rate:

<u>Measurement Year</u>	<u>(\$000's)</u>		
	<u>1% Decrease</u>	<u>Baseline</u>	<u>1% Increase</u>
June 30, 2018	\$ 25,167	\$ 28,956	\$ 33,654
June 30, 2017	26,836	30,750	35,589

Discount Rate – The discount rates used to measure the total OPEB liability as of June 30, 2018 and 2017 were 7.4% and 7.5%, respectively. Based on the assumption that plan member contributions will continue to be made at the rates specified in the Charter, it was determined that the OPEB Plan's projected fiduciary net position will be greater than or equal to the benefit payments projected for each future period. As such, the long-term expected rate of return on plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

The long-term expected rate of return on OPEB plan investments was 7.4% based on expected future returns and historical returns experienced by the Trust Fund. Expected future returns were determined based on 10-year and 20-year capital market assumptions for the Trust Fund's asset allocation. Target allocation for each major asset class and best estimates of geometric real rates of return are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long - term Expected Real Rate of Return</u>
Equities		
U.S. Equities	41.0%	7.3%
Developed Market Equity (non-U.S.)	20.0%	7.1%
Emerging Market Equity	16.0%	9.4%
Credit		
High Yield Bonds	3.0%	5.4%
Bank Loans	3.0%	5.0%
Emerging Market Bonds	3.0%	4.9%
Rate Securities		
Treasury Inflation Protected Securities	5.0%	3.3%
Investment Grade Bonds	9.0%	3.6%
Total	100.0%	

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12. Other Postemployment Benefits (OPEB) (Continued)

The asset allocation targets summarized above have a 20-year return estimate of 7.5%, which was weighted against a 10-year model estimating a 6.3% return, resulting in the ultimate long-term expected rate of return of 7.4%.

The following presents the Port’s proportionate share of the City’s net OPEB liability calculated using the discount rate, as well as what the Port’s proportionate share of the City’s net OPEB liability would be if it were calculated using a discount rate that is 1% lower or 1% higher than the current rate:

June 30, 2018 (measurement year)(\$000's)			June 30, 2017 (measurement year)(\$000's)		
1% Decrease Share of NOL @ 6.40%	Allocated Share of NOL @ 7.40%	1% Increase Share of NOL @ 8.40%	1% Decrease Share of NOL @ 6.50%	Allocated Share of NOL @ 7.50%	1% Increase Share of NOL @ 8.50%
\$ 33,290	\$ 28,956	\$ 25,409	\$ 35,227	\$ 30,750	\$ 27,079

The City issues a publicly available financial report that includes the complete note disclosures and required supplementary information related to the City’s postemployment health care obligations. The report may be obtained by writing to the City and County of San Francisco, Office of the Controller, 1 Dr. Carlton B. Goodlett Place, Room 316, San Francisco, California 94102, or by calling (415) 554-7500.

13. Receipt of the South Beach Harbor Operations

Under Assembly Bill No. X1 26 (AB26) and the California Supreme Court’s decision in California Redevelopment Association v. Matosantos, No. S194861, all redevelopment agencies in the State of California, including the Redevelopment Agency of the City and County of San Francisco (Redevelopment Agency), were dissolved by operation of law as of February 1, 2012. The Board of Supervisors adopted Resolution No. 11-12 in January 2012 to provide for the transition of assets and functions pursuant to AB26. Subsequently, in June 2012, Assembly Bill No. 1484 (AB1484) was adopted by the California Legislature. AB1484 significantly amended AB26 and impacted the transition plans initiated by the City.

A portion of the Rincon Point South Beach Harbor (SBH) Redevelopment Project Area was within Port area and the Office of Community Investment and Infrastructure, the successor agency to the Redevelopment Agency, held leasehold interests to certain Port properties.

The Port and OCII negotiated a memorandum of agreement covering the termination of Port agreements and providing for the transfer of certain assets and operations of the Rincon Point South Beach Project to the Port. In 2015, the agreement was approved by the Port’s and the OCII’s governing commissions.

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13. Receipt of the South Beach Harbor Operations (Continued)

The agreement was executed on May 1, 2019 and the Port received assets and assumed liabilities as follows:

South Beach Harbor – Port’s receipt of operations

Transferred assets	
Unrestricted cash and investments, held in City Treasury	\$ 5,078
Receivables, net	104
Depreciable capital assets, net	19,966
Total assets	25,148
Transferred liabilities	
Accrued interest payable	207
Prepaid rents and advance payments	134
Current maturities of long-term obligations	194
Lessee and other deposits	323
Long-term obligations - net of current maturities	5,950
Total liabilities	6,808
Net position of transferred operations	
Net investment in capital assets	13,499
Unrestricted	4,841
Total net position	\$ 18,340

14. Related Party Transactions

The Port receives services from, and provides services to, various City departments that are categorized in the various operating expense line items in the statements of revenues, expenses and changes in net position. The Port continues to evaluate its payments to the City’s General Fund and various City departments for services that support activities within the Port area and refine the methodologies used for the allocation of City direct and indirect costs. In fiscal year 2019, services provided by other City departments included \$2,831,000 of insurance premiums and \$611,000 in workers’ compensation expense. In fiscal year 2018, services provided by other City departments included \$2,696,000 of insurance premiums and \$544,000 in workers’ compensation expense.

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14. Related Party Transactions (Continued)

Services provided by City departments include: fireboat operations and maintenance from the Fire Department, legal and litigation-related services from the City Attorney's Office, street cleaning, direct and contractual services from the Department of Public Works, services provided by the City Purchaser, contract compliance review services by the City Administrator's Contract Monitoring Division, security services from the Police Department, risk management consulting services through the City Risk Manager, parking enforcement services and parking meter system maintenance and collection services from and through the San Francisco Municipal Transportation Agency (SFMTA), communications and network services from the Department of Technology and real estate services from the Department of Real Estate. Charges for electrical service provided by the San Francisco Public Utilities Commission (SFPUC), included in utilities on the statements of revenues, expenses and changes in net position, were \$2,074,000 and \$1,929,000 in fiscal years 2019 and 2018, respectively. Rental revenues from City departments included in operating revenues were approximately \$2,688,000 and \$2,776,000 in fiscal years 2019 and 2018, respectively.

In support of the three-year planning phase of the Embarcadero Seawall Program, the Port received \$250,000 from the Planning Department in 2019. Also, in 2019, the City provided \$250,000 for the Resiliency Plan and Improvement project. The Port received \$500,000 from SFMTA and \$250,000 from the Planning Department for project planning in 2018. In 2018, the City also provided \$3,500,000 to support the planning and design of the Mission Bay Ferry Landing.

In 2012, the Port and the SFPUC entered into a memorandum of understanding (MOU) to facilitate the installation of a shoreside power system at the Pier 70 ship repair facility. Among other things, the SFPUC committed to provide the Port a project rebate of \$1.5 million, or a pro-rata amount, based on a pre-established threshold for metered electricity consumption by the shoreside power system during the first ten years of operation. A prorated rebate amount of \$350,000 has been accrued at June 30, 2019 and \$332,000 has been accrued at June 30, 2018 as an advance receivable, a component of unrestricted other noncurrent assets.

The Port and SFPUC entered into an MOU dated September 1, 2018 to construct certain improvements to the Mariposa Pump Station and associated sewer work on the Port premises located within Seawall Lot 345. The SFPUC will use the premises for an initial term of 30 years and pay the Port rent payment of \$0.45 per square foot per month with a 3% annual increase for a total rent of \$1,242,000. In fiscal year 2019, SFPUC paid the Port a lump sum of \$502,000 as the net present value of the total rent for the initial term of 30 years.

On September 27, 2018, the Port and Mayor's Office of Housing and Community Development (MOHCD) entered into a Memorandum of Understanding to implement the affordable housing development project at the Seawall Lot 322-1 ("88 Broadway"). MOHCD agreed to pay the Port the fair market value for the property in the amount of \$14,900,000 from any source funds available to MOHCD. If MOHCD does not pay the Port the full fair market value as of the date of Ground Lease closing, interest will accrue on the unpaid amounts at a rate of 1.5% simple interest per annum during the first two (2) years and at a rate of 3% per annum thereafter until the date of payment in full. At June 30, 2019, the Port is due a total of \$14,958,000 from MOHCD. In March 2019, the Port entered into a Ground Lease with a developer. The Ground Lease has a term of fifty-seven years plus one eighteen extension option (a 75-year maximum term but with expiration

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14. Related Party Transactions (Continued)

no later than December 31, 2105). The lease revenues are being amortized over the 75-year maximum term of the lease. At June 30, 2019, the Port has a noncurrent unearned revenue balance in the amount of \$14,500,000 related to this Ground Lease. In addition to the payment by MOHCD, the Developer will be required to make lease payments representing a share of any cash flow generated by commercial activities.

The Port and Department of Building Inspection (DBI) entered into an MOU dated May 7, 2018 to provide plan review and field inspection in accordance with San Francisco Building Code on projects enforced by the Port. As of June 30, 2019, the Port accrued a liability payable to DBI in the amount of \$585,000 for the 88 Broadway project.

In December 2017, the Port and San Francisco Fire Department (SFFD) entered into an MOU for the use of water, apron, shed and office space at Pier 26 for berthing and servicing of fireboats for five years and on a month-to-month basis afterward. To facilitate these uses, SFFD repaired apron decking, replaced the fender system within the leasehold area and upgraded electrical services to Pier 26. In return, the Port allowed SFFD to apply hundred percent rent credits toward the lease payments until all required capital improvements, approximately \$2.3 million, are fully offset. As of June 30, 2019, rent credits of \$366,000 have been provided to SFFD.

15. Operating Lease Commitment

The Port has a noncancelable operating lease (sublease) for its offices at Pier 1 from the master tenant, which requires the following minimum annual payments (in thousands):

<u>Year Ending</u> <u>June 30</u>	
2020	\$ 2,726
2021	2,726
2022	2,726
2023	2,726
2024	2,726
2025-2029	13,628
2030-2034	13,628
2035-2039	13,628
2040-2044	13,628
2045-2049	13,628
2050-2054	13,628
2055-2059	13,628
2060-2064	13,628
2065	<u>227</u>
Total	<u>\$ 122,881</u>

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15. Operating Lease Commitment (Continued)

The master lease, as amended in fiscal year 2016, allows the master tenant an option to extend the lease term for an additional 15 years. Among other things, the amended provisions include a grant to the Port, as sub-lessee, a one-time early termination right in 2031, and if such termination is not exercised, a 15-year extension option, for a term coterminous with the master lease, if the master lease is also extended. The Port has an option to purchase the leasehold premises at a price equal to the present value of the remaining base rent due from the Port to the master tenant, effective through the expiration date of the sublease. Rental payments totaled \$2,725,000 in fiscal year 2019 and \$2,704,000 in fiscal year 2018.

16. Commitments

Development and Capital Projects

The Port is engaged in development and capital projects, which involve commitments to expend significant funds. Certain development plans, such as that for the Pier 70 area, require complex financing strategies including an array of public and private financing mechanisms in order to accomplish development objectives, which may include environmental remediation (see Note 17), preservation and adaptive reuse of historic buildings, and construction of new infrastructure and public open spaces.

The Port has pursued State legislative changes to increase funding options to address future capital requirements. In 2005, Senate Bill No. 1085 amended the California Government Code to enable the City and the Port to form, in the Port area, infrastructure financing districts, pursuant to Section 53395 et seq. Among other things, this legislation enumerated additional infrastructure improvements that qualify for infrastructure financing districts, including seismic upgrades, historic renovation, environmental remediation, utility improvements, and structural repair or construction of seawalls, piers, and wharves.

The 2012 San Francisco Clean and Safe Neighborhood Parks Bond general obligation bonds, included \$34.5 million and the 2008 Parks Bond included \$33.5 million of funding for parks and open space projects on Port property.

Purchase Commitments

The Port had firm purchase and contract commitments at June 30, 2019 for approximately \$21.2 million for capital projects and \$4 million for general operations.

17. Contingencies

Litigation

The Port is a defendant in various lawsuits and claims that arise during the normal course of business. Most of these matters deal with personal injury or property damage resulting from accident or fire and are covered by insurance. When the likelihood of an unfavorable outcome is probable, accrued liabilities will include, at a minimum, the aggregate amount of deductibles under

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17. Contingencies (Continued)

applicable insurance policies. There are also pending actions filed by tenants and vendors, alleging breach of leases or contracts, and associated economic losses. The final disposition of these legal actions and certain legal claims is not determinable. However, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or changes in net position of the Port.

The estimated claims payable at June 30, 2019 and 2018 is \$450,000. Two asserted claims remain open, which contributes to the Port's estimated claims liability.

Grants

Certain grants that the Port receives are subject to audit and financial acceptance by the granting agency based upon their review of costs incurred. The Port's management does not believe that such audits will have a material impact on the financial statements.

South Beach Harbor Project Commitments

On May 1, 2019, OCII transferred South Beach Harbor operations to the Port (see Note 13). Under San Francisco Bay Conservation and Development Commission (BCDC) Permit Amendment No. 17 for the South Beach Harbor Project, certain public access and other improvements were to be completed by December 31, 2017. Construction estimates prepared by a Port consultant in 2014 indicate that the required uncompleted work would cost approximately \$7.9 million. The Port has worked with the water recreation community to develop an alternative public access improvement proposal for BCDC consideration. Port management believes that the alternative proposal will provide significant public access improvements that are relevant to the project area and at a lower cost. The Port is seeking an extension of time from BCDC to complete the amended project work.

Environmental

The Port is required to comply with a number of federal, State and local laws, regulations, and permits designed to protect human health, safety and the environment. In conforming to these laws, the implementing regulations and permits, the Port has instituted a number of compliance programs and procedures. It is the Port's intent that its environmental compliance programs conform to regulatory and legal requirements while effectively managing its financial resources.

The Port's financial statements include liabilities, established and adjusted periodically, based on new information, in accordance with applicable generally accepted accounting principles in the United States of America, for the estimated costs of compliance with environmental laws and regulations and remediation of known contamination. As the Port undertakes future development planning, the Port evaluates its overall provisions for environmental liabilities in conjunction with the nature of future activities contemplated for each site and, if necessary, accrues a liability. It is, therefore, reasonably possible that in future reporting periods current estimates of environmental liabilities could materially change.

Port lands are subject to environmental risk elements typical of sites with a mix of light industrial activities dominated by transportation, transportation-related and warehousing activities. Due to the historical placement of fill of varying quality, and widespread use of aboveground and underground tanks and pipelines containing and transporting fuel, elevated levels of petroleum

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17. Contingencies (Continued)

hydrocarbons and lead are commonly found on Port properties. Consequently, any significant construction, excavation or other activity that disturbs the soil, fill material or bay sediment may encounter hazardous materials and/or generate hazardous waste.

The Port has identified certain environmental issues related to Port property, including asbestos removal, fuel tank removal, and oil contamination. The Port may be required to perform certain clean-up work if it intends to develop or lease the property, or at such time as required by the City or State. There are sites where groundwater contamination may be later identified, where the Port has primary or secondary responsibility. The potential liability for all such risk cannot be reasonably made at this time.

Pier 70 – For over 150 years there were ironworks, steelworks, shipbuilding and repair, and other industrial operations at this 69-acre site. Between 2007 and 2010 the Port conducted a comprehensive community-based planning process for the redevelopment of Pier 70. This culminated in the Preferred Master Plan for Pier 70 involving rehabilitation and reuse of the historical buildings, preservation of ship repair facilities, new development, park and open space, and pollution remediation.

Between 2009 and 2013, with financial assistance from the U.S. Department of Commerce, the Port completed a comprehensive investigation of soil and groundwater conditions, a risk assessment and feasibility study, and a Remedial Action Plan (RAP). The RAP consists of capping site soils and establishing institutional controls to reduce or eliminate human health risks related to contamination. The Port subsequently developed a Risk Management Plan (RMP), which established institutional controls (e.g. use restrictions, soil handling requirements, health and safety plans, etc.) and engineering controls (e.g. capping contaminated soil) to protect the public and prevent an adverse impact to the environment. The RMP specifies how future development, operation, and maintenance of the area will implement the remedy, by covering existing site soil with buildings, streets, plazas, hardscape, or new landscaping, thereby minimizing or eliminating exposure to contaminants in soil. The Regional Water Quality Control Board approved the RMP in January 2014.

Previous investigation of the northeast shoreline of Pier 70, discovered near-shore sediments containing PCBs and polycyclic aromatic hydrocarbons (PAH) at concentrations that pose a potential risk to aquatic life and human health under certain exposure scenarios, and require removal or capping of sediment before the development of the area for public access and recreation. Environmental consultants to the Port prepared a preliminary cost estimate, for installation of a chemical isolation cap consisting of an activated carbon-based treatment media and gravel/rock layer over the impacted area. In 2018, the Port entered into a disposition and development agreement with a developer for the 28-acre Waterfront Site. The developer assumes substantial responsibility for capping contaminated soil in the project area in accordance with the RMP.

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17. Contingencies (Continued)

Cost estimates are evaluated annually based on additional information and transaction events that impact the pollution remediation outlays that are expected to be incurred by the Port. The accrued cost for pollution remediation at Pier 70 is estimated to be \$4,105,000 on June 30, 2019, and \$3,000,000 on June 30, 2018. The \$3,000,000 obligation as of June 30, 2018, represents the estimated cost to remediate contaminated sediment at the Crane Cove Park project. In the fiscal year 2019, the obligation to install a durable cover over unpaved native soil at Pier 70 became applicable to a 4-acre upland area located south of Crane Cove Park and north of the former Pier 70 Ship Repair facility. The estimated cost to cover this upland soil is \$1,105,000, resulting in the \$4,105,000 obligation on June 30, 2019. The June 30, 2019 obligation represents the estimated cost to remediate contaminated sediment at the Crane Cove Park project and an undeveloped upland area approximately four acres within the Pier 70 master plan area.

Former Pier 64 Marine Terminal Investigation & Remediation - A 2017-2018 investigation of sediment quality in the former Pier 64 area found elevated concentrations of polycyclic aromatic hydrocarbons (PAHs) in land sediments owned by the Port. In August 2019, the San Francisco Bay Regional Water Quality Control Board (Water Board) issued a directive (under Clean Water Act Section 13267) to conduct further investigation and evaluation of sediment contamination near the former Pier 64. This directive constitutes a regulatory order and it identified a group of potentially responsible companies. These companies or their predecessors discharged petroleum products into waters of the state. The Port of San Francisco is named in this directive because it is the current property owner.

Based on information available to date, the Port believes that contamination in the Pier 64 sediment is primarily attributable to historic oil company operations, fires and fuel releases, and the former Southern Pacific freight slip operating on the north side of Pier 64. However, as the PAH contamination may not be fully attributable to historic oil companies and railroad operations, it is possible that the Port may be partially liable for some future investigation or remediation costs. As the information available to date is preliminary, the extent of Port's potential liability cannot reasonably be made at this time.

Mission Bay Ferry Landing (MBFL) - The Port's Mission Bay Ferry Landing (MBFL) Project is located adjacent to the south side of the former Pier 64. The MBFL project consists of approximately 7.9 acres of in-water area, dredging, ferry berths, 340 feet of armored shoreline, and land-side improvements extending approximately 65 feet inland from the shoreline.

While planning the MBFL Project, the Port analyzed sediment and found elevated concentrations of PAHs in sediment in a portion of the MBFL proposed dredge area. As required by the regulatory and resource agencies that authorize in-water construction and dredging, the Port completed a feasibility study in June 2018. The feasibility study evaluated the potential environmental impacts of dredging, construction activities, and the impact on aquatic organisms. The study proposed a sediment cap where residual PAHs would remain. The final project engineering plans include removal of the upper portion of contaminated sediment and placement of a 1.6-acre sediment cap.

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17. Contingencies (Continued)

The PAH contamination may be largely attributable to historic operations by the Pier 64 potentially responsible companies. However, the Port is proceeding with plans to remediate the sediment contamination as part of the MBFL project. In the future, the Port may seek to recover costs incurred during the MBFL project from the Pier 64 potentially responsible companies. As the PAH contamination may not be wholly attributable to historical operations, the Port might be liable for some of the investigation and/or sediment cap construction costs. As the information available to date is preliminary, the extent of Port’s potential liability cannot reasonably be made at this time.

PG&E Bankruptcy – For nearly two decades, the Port has worked closely with the Pacific Gas & Electric Company (PG&E) and regulatory agencies such as the San Francisco Bay Regional Water Quality Control Board to investigate, plan, and remediate pollution along Port lands resulting from PG&E’s (or its predecessor’s) operation of power plants (e.g. Potrero Power Plant, Hunter’s Point Power Plant) and manufactured gas plants (e.g. Beach Street MGP) on or near Port property. Due to the historical activity and operations of these PG&E plants, there is environmental contamination in soil and sediments within Port jurisdiction. In these cases, the Port has legal claims against PG&E as a result of the contamination. Port has not actively pursued these legal claims and they have not been disclosed in recently issued Port financial statements because PG&E, as the culpable party, has complied with all regulatory directives to address the contamination and the Port’s liability, solely as an owner. Given PG&E’s responsiveness, the probability of a Port obligation was determined to be remote.

PG&E filed bankruptcy in January 2019. Despite the bankruptcy PG&E has continued to cooperatively address the ongoing environmental investigation and remediation efforts as planned. Port staff is working with the City Attorney’s Office to monitor PG&E’s activities and authority to continue work and make payments related to environmental cleanup. In March 2019, the bankruptcy court issued an order allowing PG&E to continue its customer programs, including its environmental cleanup programs. The Port will include all environmental claims in the City’s bankruptcy claim against PG&E. As the information available to date is preliminary, the extent of Port’s potential liability cannot reasonably be made at this time. Therefore, as of June 30, 2019, no additional pollution remediation accrual has been made.

A summary of environmental liabilities, included in noncurrent liabilities, at June 30, 2019 and 2018, is as follows (in thousands):

	Environmental Remediation	Miscellaneous Compliance	Total
Environmental liabilities at July 1, 2017	\$ 11,211	\$ 231	\$ 11,442
Current year claims and changes in estimates	(8,211)	-	(8,211)
Vendor payments	-	(187)	(187)
Environmental liabilities at June 30, 2018	<u>\$ 3,000</u>	<u>\$ 44</u>	<u>\$ 3,044</u>
Environmental liabilities at July 1, 2018	\$ 3,000	\$ 44	\$ 3,044
Current year claims and changes in estimates	1,105	-	1,105
Environmental liabilities at June 30, 2019	<u>\$ 4,105</u>	<u>\$ 44</u>	<u>\$ 4,149</u>

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18. Risk Management

Insurance – General and Workers' Compensation

The Port is subject to various risk of loss, including general liability, property and casualty, and workers' compensation. The Port carries commercial insurance for all risks of loss with the following exceptions: (i) workers' compensation; (ii) property damage to most Port owned vehicles; (iii) employee health and accident; (iv) professional liability; and (v) losses due to seismic events.

More specifically, the Port carries the following insurance (listed coverage limits and related deductible amounts are effective July 1, 2019): (i) marine general liability coverage of \$100.0 million, subject to a deductible of \$100,000 per occurrence; (ii) hull and machinery liability coverage of \$1.1 million, subject to a deductible of \$100,000 per occurrence; (iii) commercial property insurance for losses up to the insured appraised value of Port facilities, subject to a maximum of \$1.0 billion and a deductible of \$750,000 per occurrence (\$150,000 per occurrence for the Port's cargo cranes); and (iv) public officials and employee liability coverage of \$5.0 million, subject to a deductible of \$50,000 per occurrence. The Port also carries insurance coverage for employee dishonesty, auto liability, property damage for certain high-value Port vehicles, water pollution, and data processing equipment. In addition to the above, the Port requires its tenants, licensees, and contractors on all contracts to carry commercial general liability insurance in various amounts naming the Port Commission and the City as additional insured parties. Tenants whose operations pose a significant environmental risk are also required to post an environmental oversight deposit and an environmental performance deposit.

Losses from workers' compensation claims of Port employees, the deductible portion of insured losses, and losses from other uninsured risks must be funded by current revenues or reserves. The administration of workers' compensation, including estimates of recorded and incurred but not reported claims, is provided by the City. The workers' compensation liability as of June 30, 2019 and 2018 has been evaluated by an independent actuary.

With respect to the general liability accrual, the Port has various unsettled lawsuits filed, or claims asserted against it as of June 30, 2019 and 2018. The Port's General Counsel and management have reviewed these claims and lawsuits in order to evaluate the likelihood of an unfavorable outcome to the Port and to arrive at an estimate of the amount or range of potential loss to the Port. Claims liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. The estimate for claims liability depends on complex factors, such as inflation, changes in legal doctrines, newly discovered information and historical damage awards. Claims are reevaluated periodically to consider such factors and recent claims settlement trends (including frequency and amount of pay-outs). The estimate of the claims liability also includes increases or decreases to previously reported unsettled claims. The general liability reserve is included in estimated claims payables.

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18. Risk Management (Continued)

Changes in the reported liability reserves for June 30, 2019 and 2018 resulted from the following activity (in thousands):

	General Liability		Workers' Compensation	
	2019	2018	2019	2018
Beginning of year	\$ 450	\$ 1,125	\$ 3,000	\$ 2,906
Current year claims & changes in estimate	30	(663)	159	638
Settlements	(30)	(12)	(611)	(544)
End of year	\$ 450	\$ 450	\$ 2,548	\$ 3,000

19. Subsequent Events

In September 2019, the Port executed documents, pursuant to Section 2.14 of the Port's Revenue Bond Master Indenture ("Master Indenture"), which made effective the Port Commission's earlier designation of the Pier 70 Special Use District (SUD) and Mission Rock Project Site as Special Facilities under Section 2.14 of the Revenue Bond Master Indenture. The revenues from the Pier 70 SUD and Mission Rock Project Site constitute Special Facility Revenues and are not included in the Net Revenues pledged to the Revenue Bonds.