Office of the Auditor General

OFFICE OF THE AUDITOR GENERAL

250.1

SAN FRANCISCO PORT COMMISSION
INTERIM REPORT ON
PROJECTED CASH DEFICITS

DECEMBER 1974

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December 4, 1974

The Honorable Speaker of the Assembly
The Honorable President of the Senate
The Honorable Members of the Senate and the
Assembly of the Legislature of California

Members:

Transmitted herewith is the Auditor General's interim report pertaining to the immediate and long-term projected cash deficits of the San Francisco Port Commission.

The port will have insufficient cash to meet all of its debts, including payments to employees and creditors such as the State of California, during the month of June 1975. As of June 30, 1975, the cash deficit will be approximately $680,000.

The cash deficit can be avoided in the month of June 1975 by not expending all of the funds budgeted in fiscal year 1974-75 for equipment, maintenance, improvements and reconstruction of port facilities. The Acting Port Director has made only limited expenditures for these items, and has not filled vacant positions in order to avoid a possible deficit in June 1975.

However, even if the port, through its present measures of deferring expenditures, meets its debts for the month of June 1975, the port will be only postponing the cash deficit, which is projected to exceed $3 million as of June 30, 1976.

The cash projected by the port to be available as of June 30, 1982 is overstated by approximately $24.8 million. While the port projected a cash balance of approximately $3.5 million as of June 30, 1982, the Auditor General has projected that, on the contrary, the port will need an additional $21.3 million over the period July 1, 1974 through June 30, 1982.

The port's cash flow projection has overstated interest income by $10.9 million, has overstated tenant revenues by $9.9 million and has understated operating expenditures by $4 million, representing total cash overstatements of $24.8 million.

Suggested alternatives are listed in the report to resolve the port's cash flow problems. These alternatives include the use of non-port city and county revenues such as additional revenue sharing allocations or ad valorem tax monies to assist in the port's financing. Such alternatives also include temporary authorization by the State Legislature for the state, in lieu of the port, to pay the bond interest and redemption costs of the state bonds issued for port purposes. An additional $29 million is to be paid to the state by the port before June 30, 1982.

The Auditor General has recommended that the San Francisco Port Commission formulate a policy to resolve the port's current and long-term cash deficit problems. Policy considerations should include discussions with and appropriate requests from the Mayor and the Board of Supervisors of the City and County of San Francisco.

Respectfully submitted,

Vincent Thomas

VINCENT THOMAS, Chairman
Joint Legislative Audit Committee

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INTRODUCTION

In response to a legislative request, we are in the process of performing a management audit of the San Francisco Port Commission, which was transferred from the state to the City and County of San Francisco on February 6, 1969. An interim report pertaining to the immediate and long-term projected cash deficits of the port is being issued at this time.

Port policy is established by the San Francisco Port Commission, consisting of five persons appointed by the Mayor subject to confirmation by the Board of Supervisors, for terms of four years each.

The port's operating cash balance has been reduced from $10 million, at the time of the 1969 transfer of the port from the state to the City and County of San Francisco, to $1 million at June 30, 1974.

The Acting Port Director, as the chief executive of the port, is responsible for the port's day-to-day administrative activities.

The City and County of San Francisco, including the Acting Port Director and the Budget Analyst of the Board of Supervisors, have cooperated with us fully during the course of our audit.

FINDINGS

THE PORT WILL HAVE INSUFFICIENT CASH TO MEET ALL OF ITS DEBTS, INCLUDING PAYMENTS TO EMPLOYEES AND CREDITORS SUCH AS THE STATE OF CALIFORNIA, DURING THE MONTH OF JUNE 1975. AS OF JUNE 30, 1975, THE CASH DEFICIT BALANCE WILL BE APPROXIMATELY $680,000. EVEN IF THE PORT, THROUGH ITS PRESENT MEASURES OF DEFERRING EXPENDITURES, MEETS ITS DEBTS FOR THE MONTH OF JUNE 1975, THE PORT WILL ONLY BE POSTPONING THE CASH DEFICIT, WHICH IS PROJECTED TO EXCEED $3 MILLION AS OF JUNE 30, 1976.

Our cash flow projections show that the port will not have sufficient cash to meet its fiscal year 1974-75 obligations sometime in June 1975. Based on normal expenditures necessary to operate and maintain the port, there will be a cash deficit of approximately $680,000 as of June 30, 1975. However, the cash deficit can be avoided in the month of June 1975 by not expending all of the funds budgeted for fiscal year 1974-75 for maintenance, improvements and reconstruction of port facilities and for purchases of equipment. In order to avoid a possible deficit in June 1975, the Acting Port Director has made only limited expenditures in these areas, and has effected other cash savings by not filling vacant positions.

If the port is able to meet its obligations in the month of June 1975, it will only do so by operating at a lower-than-normal level. It will be faced with starting fiscal year 1975-76 with little or no available cash. The port must then not only meet its current expenditures but also should pay for all necessary costs postponed from the fiscal year 1974-75. Based on our analysis of estimated revenues and expenditures for fiscal year 1975-76, we project a cash deficit in excess of $3 million by the end of that fiscal year. This projection assumes that the port does not pay for any of the expenditures deferred in the current fiscal year of 1974-75.

The following schedule, rounded to the nearest $5,000, compares the cash flow statement prepared by the port with our revised cash flow statement based on anticipated revenues and expenditures.

	Port Projection		Auditor General Projection	
Beginning cash balance as of 7/1/74		$1,055,000*		$1,055,000*
Revenues	$16,035,000		$14,485,000	
Less expenditures	(16,090,000)		(16,220,000)	
Excess of expenditures over revenues		(55,000)		(1,735,000)
Ending port cash balance and Auditor General cash deficit balance as of 6/30/75		$1,000,000		$ (680,000)

* Excludes $260,000 in revolving funds.

The cash balances in the above schedule include $270,000 of restricted cash which may not be available during this period because of a legal action involving the federal government. In addition, in prior years, the port has had difficulty collecting revenues from one of its tenants. If similar difficulties are encountered from any of its tenants during 1974-75, the cash deficit will be greater.

As a result of the port's current inadequate cash position, it will be unable to pay all of its employees and creditors, including the State of California, in the month of June 1975, except by deferring operating and capital expenditures. Deferring these expenditures will only postpone the time until the 1975-76 fiscal year when we project the port will be unable to pay all of its obligations. As previously noted, we project a cash deficit in excess of $3 million by June 30, 1976.

With regard to the obligations due to the State of California, the port, pursuant to Section 9, Chapter 1333 of the Statutes of 1968, as amended, must transfer to the state amounts necessary to pay bond indebtedness of state general obligation bonds issued for San Francisco Harbor improvement. During fiscal year 1974-75, the port must pay to the state approximately $4.1 million to meet bond interest and redemption. Over $29 million must be paid to the state by the port before June 30, 1982. To date, the port has paid the state approximately $23 million for such bond interest and redemption.

THE CASH ESTIMATED BY THE PORT TO BE AVAILABLE AS OF JUNE 30, 1982 IS OVERSTATED BY APPROXIMATELY $24.8 MILLION. THEREFORE, IT IS PROJECTED THAT THE PORT WILL NEED AN ADDITIONAL $21.3 MILLION OVER THE PERIOD JULY 1, 1974 THROUGH JUNE 30, 1982.

The projected cash flow statement which was prepared by the Port Controller and included in a different format in the October 2, 1974 report of the Budget Analyst of the San Francisco Board of Supervisors shows that the port will have sufficient cash available to meet its expenses through June 30, 1982.

The following schedule, rounded to the nearest $5,000, compares the cash flow statement prepared by the port with our revised cash flow statement based on anticipated revenues and expenditures.

	Port Projection		Auditor General Projection	
Beginning cash balance as of 7/1/74		$1,055,000*		$ 1,055,000*
Revenues	$148,180,000		$127,035,000	
Less expenditures	145,760,000		149,390,000	
Excess (Decrease) of revenues over expenditures		2,420,000		(22,355,000)
Ending port cash balance and Auditor General cash deficit balance as of 6/30/82		$3,475,000		$(21,300,000)

*Excludes $260,000 in revolving funds.

Therefore, the cash balance estimated by the port to be available as of June 30, 1982 is overstated by approximately $24.8 million, with the result that the port will need an additional $21.3 million over the period July 1, 1974 through June 30, 1982. The following schedule recaps this overstatement.

Port cash balance projection as of June 30, 1982	$ 3,475,000
Auditor General cash deficit projection as of June 30, 1982	(21,300,000)
Amount by which port cash projection is overstated	$24,775,000

The port projection is based on the prior years' experience, the budget for the current fiscal year, and assumptions regarding the future. In our judgment, three of these assumptions are in error.

Overstatement of Interest Income -- $10.9 Million

Interest income earned for fiscal year 1973-74 was approximately $1.8 million, or 13 percent of the port's total revenues in 1973-74. That fiscal year was used as the basis for future projections. The 1973-74 total revenue receipts of $13.6 million, including the $1.8 million of interest income, were projected by the port to increase to $16 million during fiscal years 1974-75 and 1975-76 and then continue to increase at the annual rate of $500,000 through June 30, 1982. The port's cash flow statement, therefore, assumes either:

- That interest income will remain at least at $1.8 million annually, or

- There will be other unidentified revenues which will offset any reduction of this interest income.

The port was unable to furnish us with documentation to support the other unidentified revenues.

With regard to interest income, most of the $1.8 million of interest income in fiscal year 1973-74 was earned on $20 million of the $34 million general obligation bond issue, which was sold on May 1, 1973. None of the $20 million had been expended as of July 1, 1973 and the unexpended balance as of June 30, 1974 was $14.8 million.

At the present rate of bond fund expenditures, the balance remaining and therefore earning interest income at the end of this fiscal year is estimated to be $6.5 million. In addition, with the cash balances in the operating and bond sinking funds now substantially below the balances of a year ago, interest earnings for the current fiscal year of 1974-75 are estimated to be $1 million rather than the $1.8 million of last year.

If the remaining $14 million of the $34 million general obligation bond issue is sold before July 1, 1975, interest earnings would increase to $1.5 million during 1975-76. However, interest earnings during subsequent years would be substantially reduced as the bond funds are expended on port improvements. Based on the prior and present rate of bond fund expenditures, we estimate that the interest earnings through June 30, 1982 to be $3.5 million rather than the $14.4 million included in the port's cash projection. Therefore, interest income has been overstated by $10.9 million through June 30, 1982.

Overstatement of Tenant Revenue -- $9.9 Million

The port's cash projection through June 30, 1982 includes approximately $9.9 million in tenant revenues which the port will not receive. Therefore, these revenues have been overstated by $9.9 million through June 30, 1982.

Understatement of Operating Expenditures -- $4 Million

The budgeted operating expenditures for the current fiscal year of 1974-75 are $500,000 below the actual expenditures incurred in the prior year.

While the Acting Port Director, through not filling vacant positions and through deferring other expenditures, may meet this budget, our projection, using the prior actual experience of operating costs, shows that the operating expenditures as projected by the port have been understated by $4,000,000 through June 30, 1982.

Suggested Alternatives for Resolving Cash Problem

Following are suggested alternatives to resolve the port's cash flow problem. While such alternatives should be considered, none is a specific recommendation of the Auditor General at this time.

- Police, fire and street maintenance costs of approximately $1.1 million annually which have been paid from port operating revenues could be paid from other city and county revenues.

- The possessory interest tax revenues now derived by the city and county from port tenants could be paid to the port.

- The approximate $7 million of the $10 million operating cash balance transferred from the state to the city in 1969 which has been expended by the port for capital improvements could, if legal, be used as the basis for a temporary loan from the port's general obligation bond funds to the port's operating funds. The bond funds were authorized for capital improvements.

- The amount of the federal revenue sharing funds allocated to the port could be increased.

- The State Legislature could be requested to authorize, on a temporary basis, that bond interest and redemption payments on state bonds, which were issued for port purposes, be made from state funds rather than port funds. As previously noted, over $29 million must be paid to the state by the port before June 30, 1982.

- A direct appropriation could be made out of the city and county's ad valorem tax revenues for the port.

We conclude that the port does not have sufficient cash available to efficiently meet its obligations through June 30, 1975. In addition to the immediate cash problem, the long-range cash projection of the port through June 30, 1982 overstates the amount of available cash by approximately $24.8 million, with the result that the port will need an additional $21.3 million over the period July 1, 1974 through June 30, 1982.

The Acting Port Director has previously advised the port commission that the port is faced with both short-term and long-term cash problems.

RECOMMENDATION

We recommend that the San Francisco Port Commission formulate a policy to resolve the port's current and long-term cash deficit problems. Policy considerations should include discussions with and appropriate requests from the Mayor and the Board of Supervisors of the City and County of San Francisco.

BENEFITS

Proper implementation of this recommendation should result in the resolution of the port's cash flow problems.

SUMMARY OF COMMENTS
OF THE ACTING PORT DIRECTOR AND HIS STAFF

1. We substantially concur with the findings contained in the report.

2. However, with regard to the cash estimated to be available as of June 30, 1982, there are too many future uncertainties to determine the validity of any such long-term cash flow projection at this time.

3. Revenues contained in the port's projected cash flow statement did not identify individual revenue components such as interest income. Rather, projections of total revenues were based on the prior growth experience of the port.

4. Subsequent appropriate actions by port management should eventually resolve the port's cash flow problems.

Harvey M. Rose
Harvey M. Rose
Auditor General

Date: December 3, 1974

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