

2016-2020 Draft Plan of Finance

A. Introduction

The Port of Seattle underwent a number of organization changes in 2015, including both the formation of the Northwest Seaport Alliance and an internal divisional reorganization. The Port operates very distinct businesses and the recent organizational changes are designed to provide focus on specific businesses while also breaking down divisional silos and creating a single organization with a common purpose. This will better assist the Port achieve its Century Agenda strategic goals and objectives while furthering its mission to create jobs by advancing trade and commerce, promoting industrial growth, and stimulating economic development.

U.S. economic growth remains moderate heading into 2016. The US stock market has remained largely flat in 2015, while the national unemployment rate is down to 5.0% from its 10% peak in 2009. However, the U.S. economy continues to produce somewhat stagnant wage growth, and the impacts of the expected Federal Reserve interest rate hikes are still unknown. Globally, concerns remain over the ongoing unrest in the Middle East, along with economic slowdowns in Europe and Asia, particularly in China and Japan, which are the world's second and third-largest economies, respectively. The Puget Sound region, however, continues to benefit from above-average income levels, steady population growth, and robust job growth. The unemployment rate in King County was down to 3.9% in September 2015, making it the lowest in the state and well below the national level. The Port, particularly SeaTac, benefits directly from this strong regional economic base.

SeaTac Airport is on pace for its sixth consecutive year of enplanement growth, with an increase of 12.5% forecasted in 2015; it is expected to be the fastest growing airport in the country. From a regional perspective, the airport continues to benefit from being the primary air passenger service provider in the Seattle area, its geographic location as a natural gateway to Asia, and a vibrant regional economy. Additionally, the airline industry is expected to be profitable in 2015 for the sixth year in a row. Airline domestic capacity in 2015, as measured by available seats, is reaching its highest level in seven years, and international seats are at an all-time high. Demand for air travel is driven by an expanding economy, employment growth, rising personal income and higher consumer sentiment. The Aviation division accounts for over 75% of the 2015 forecasted Port-wide revenues and almost 90% of the 2016-2020 Capital Improvement Plan (CIP).

The Port's container business continues to experience intense competition from other West Coast ports, as well as those in the East and Gulf Coasts, Mexico and Canada. Shipping lines and terminal operators are exploring ways to reduce costs, including introducing larger vessels, forming stronger alliances, and consolidating terminals to gain economies of scale. To combat these challenges, the Port of Seattle and the Port of Tacoma jointly formed the Northwest Seaport Alliance (NWSA) in August 2015, creating unified management of the third largest container gateway in North America.

The NWSA was formed as a Port Development Authority, which is a separate legal entity from the individual ports. The Ports of Seattle and Tacoma have licensed certain marine cargo facilities to the NWSA, which will act as the exclusive manager and operator of the marine cargo business of both ports. The individual ports retain their existing port commission governance structures, budgeting, ownership of licensed assets, debt, and obligations for repayment of port debt. However, under NWSA management, the two ports' marine cargo terminal investments, operations, planning and marketing efforts are unified with the goal of strengthening the Puget Sound gateway, including a focus on ensuring that container facilities will be able to handle the larger ships migrating into the trans-Pacific trade. The Pacific Northwest is a key region for inbound and outbound United States cargo, moving cargo not only for regional trade, but also cargo headed to destinations throughout the Midwest. Combining the cargo

terminal operations is expected to make the region more competitive in the global economy and create new jobs in Washington State. The NWSA represents the third-largest trade gateway in North America, behind only the ports of Los Angeles and Long Beach and the Port of New York/New Jersey. Through July 2015, the two ports handled nearly 2.1 million TEUs, a 4% increase year-to-date, and \$42.4 billion of trade.

The NWSA will distribute cash to each Port based on cash flow from operations, calculated pursuant to General Accepted Accounting Principles (GAAP). Cash distributions will be made no less than quarterly based on each Port's percentage of total shares. The NWSA is treated as a joint venture for accounting purposes and the Port expects to recognize as Gross Revenue its share (initially 50 percent) of the NWSA Net Income or Losses (as defined in the NWSA Charter to mean, for each fiscal year or other period, an amount equal to the Seaport Alliance's net operating income or losses less depreciation plus non-operating income or losses, determined in accordance with GAAP). For additional information on the NWSA, please refer to Section XII, "The Northwest Seaport Alliance 2016 Budget", or visit their website:

<https://www.nwseaportalliance.com>

As discussed above, the Port revised its organizational structure in 2015. Airport operations will continue to report under the Aviation division, while Non-Airport operations are now reported under a new structure. The properties and related operations now licensed to the NWSA were previously reported under the former Seaport division, which along with the former Real Estate division was eliminated under the new organization structure. Other former Seaport division businesses and facilities, including cruise, grain and certain other properties have been formed into the new Maritime division, along with recreational and commercial marinas, which were formerly part of the Real Estate division. A newly created Economic Development division now includes the management of former commercial properties, also formerly of the Real Estate division, and also will have responsibility for the Port's broader economic development activities, including real estate portfolio management and property development, tourism and social responsibility initiatives (both formerly part of administrative services), and a new small business "incubator". In addition to the Port's operating divisions, several port departments provide corporate and capital development services to the operating divisions; the costs associated with these services are allocated to the operating divisions.

For the purposes of the Plan of Finance discussion below and the overarching capital funding approach, the Port segregates *Airport* (i.e. *Aviation*) operations from *Non-Airport* operations. Non-Airport operations are inclusive of Maritime, Economic Development, and the Port's share of the NWSA.

The 2016 budget and the 2016-2020 forecasts are based on continued sound fiscal management, which include prudent expense management and maintenance of strong financial margins and liquidity.

B. Selected Financial and Operating Information

TABLE X-1: FINANCIAL SUMMARY – PORTWIDE (\$ millions)

		2015	2016
	2014 Actual	Forecast ⁽¹⁾	Budget ⁽²⁾
OPERATING REVENUES			
Aviation Operating Revenues	\$ 406.1	\$ 421.7	\$ 465.8
Non-Aviation Operating Revenues	128.9	132.2	118.8
Total Operating Revenues	\$ 534.9	\$ 553.9	\$ 584.6
OPERATING EXPENSES			
Aviation Operating Expenses	\$ 230.7	\$ 239.9	\$ 268.2
Non-Aviation Operating Expenses	78.6	78.4	67.8
Total Operating Expenses	\$ 309.3	\$ 318.3	\$ 336.0
NOI Before Depreciation	\$ 225.6	\$ 235.6	\$ 248.6

(1) 2015 Forecasted figures are based on updates through Q3-2015.

(2) The 2016 budgeted Non-Aviation operating *revenues* include the Port's share of NWSA *net income* (i.e. "NWSA Distributable Revenue"), which is after the payment of operating expenses formerly paid by the Port and now paid by the NWSA. As a result, the 2016 budgeted Non-Aviation operating revenues and expenses are both lower for 2016 budget purposes. As such, NOI (revenues less expenses) would provide a better comparison of year-over-year financial results for the non-aviation businesses.

2015 Port-wide financial results, as measured by Net Operating Income (NOI) before depreciation, are currently forecasted to increase by approximately \$10.0 million from 2014. This increase includes a \$19.0 million increase in Port-wide operating revenues offset by a \$9.0 million increase in Port-wide operating expenses. The major driver of the higher 2015 forecasted NOI is the Aviation division, which forecasts a \$6.5 million increase in NOI relative to 2014, and due largely to strong non-aeronautical revenue forecasts tied to strong 2015 forecasted enplanement growth. The Port's 2016 budgeted NOI is \$13.0 million, or 5.5%, higher relative to the 2015 forecast, and is also driven largely by the Airport's rapid growth. The airport anticipates continued strong passenger growth and spending at SeaTac in 2016, but also higher operating and capital costs (costs related to the Port's aeronautical operations will be recovered from the airlines in the form of aeronautical revenues). A more detailed assessment of divisional financial results is presented below.

Please refer to Section I "Executive Summary" and Section III "Budget Overview" for more information on the Port's operating and capital budget approach and highlights.

AVIATION

2015 was the third year of the Airport's five-year airline agreement (SLOA III). Unless extended or terminated earlier, SLOA III will expire on December 31, 2017. The expiration of SLOA II resulted in a one-time (2013) revenue recognition of approximately \$18 million associated with the airline lease security deposit requirement; these funds reverted to the Port in 2013. Under SLOA III, the Port agreed to reduce the 2013 airline rates by the same amount of \$18 million; however, for accounting purposes this reduction is reflected as a straight-line revenue reduction of \$3.6 million annually in each of the five years of SLOA III.

SLOA III reflects a cost recovery model for airline-utilized property and facilities at the Airport. SLOA III provides for the sharing of a portion of Airport net income with the airlines if debt service coverage on Airport related debt exceeds 1.25 times, however the Airport can charge the airlines additional debt service coverage if Airport coverage is below 1.25 times. SLOA III also cost recovery on cash-funded assets through an amortization calculation including assets placed in service from 1992 on. The Airport assumes the risk of any vacant non-airline space, in addition to any vacant publicly accessible airline office or club space. A Majority-in-Interest of the airlines can delay new project construction, but not design, for up to 12-months.

TABLE X-2: FINANCIAL SUMMARY – AVIATION DIVISION (\$ millions)

		2015	
	2014 Actual	Forecast ⁽¹⁾	2016 Budget
Aeronautical Revenue	\$ 228.9	\$ 231.3	\$ 261.0
SLOA Adjustment	(3.6)	(3.6)	(3.6)
Non-Aeronautical Revenue			
Parking	57.1	62.6	66.8
Rental Cars	46.1	45.7	48.2
Airport Dining & Retail	47.0	50.8	54.4
Other	30.6	35.0	38.9
Total Non-Aeronautical Revenue	\$ 180.8	\$ 194.0	\$ 208.3
Total Revenue	\$ 406.1	\$ 421.7	\$ 465.8
Expenses	230.7	239.9	268.2
NOI Before Depreciation	\$ 175.4	\$ 181.9	\$ 197.5
CPE	\$ 11.48	\$ 10.25	\$ 11.00

(1) 2015 Forecasted figures are based on updates through Q3-2015.

Through October 2015, domestic and international enplanements were up 12.9% and 14.7%, respectively, as compared to the ten months ending October 31, 2014. Total passenger enplanements are forecasted to be up 12.5% in 2015 compared to 2014. This growth has been driven by a strong local economy and by Delta Airlines decision to make Seattle its West Coast hub.

The Aviation division forecasts increased total operating revenues in 2015 of \$15.6 million, which consists of increased forecasted aeronautical revenues of \$2.4 million and increased non-aeronautical revenues of \$13.2 million. The increase in aeronautical revenues, which are based on cost recovery, is due largely to increased operating expenses and capital assets placed into service, resulting from increased airline activity and growth at SeaTac, partially offset by an increased revenue sharing forecast in 2015 over 2014. The increase in revenue sharing stems from the strong 2015 forecasted non-aeronautical revenues, resulting from increased passenger volumes and spending at SeaTac, with strong performance particularly in public parking and steady growth in airport dining & retail operations (formerly “concessions”). The Aviation division, however, also forecasts \$9.2 million in increased total operating expenses in 2015, due primarily to increased baseline payroll and outside services expenses, as well as higher environmental remediation liability charges and increased allocated corporate operating expenses.

2016 Aviation total operating revenues are budgeted to increase 10.4% from the 2015 forecast as a result of increases in both aeronautical and non-aeronautical revenues. The increased budgeted aeronautical

revenues are the result of increased (recovered) operating costs and charges for capital investment, e.g. debt service, partially offset by higher anticipated revenue sharing with the airlines. The increased budgeted non-aeronautical revenues, as mentioned above, are driven by increased passenger enplanements and spending per passenger. For 2016, the Port is budgeting passenger growth of 5.5% from the 2015 forecast, with a 1.9% long-term growth forecast from 2017-2020. Total Aviation operating revenues are partially offset by an increase in budgeted operating expenses in 2016 primarily related to increased payroll costs and increased allocated corporate operating expenses.

For additional details about the Aviation division's revenues and expenses, please see Section IV "Aviation."

NON-AVIATION

As discussed above, the Port of Seattle's non-aviation operations underwent significant realignment in 2015. Fundamentally, however, the Port still derives its income from the same core businesses, the largest being leasing of container terminals, which are now managed through the NWSA. The Port continues to manage its existing non-aviation businesses, including but not limited to cruise, bulk grain cargo, recreational marinas and its real estate portfolio, although those businesses were realigned in 2015.

From an external financial reporting perspective, the Port's existing organization structure (i.e. Seaport and Real Estate) is the basis for both the 2014 and 2015 CAFR. Beginning in 2016, the Port will report externally under the new organization structure (Maritime, Economic Development, and the Port's share of the NWSA, referred to below as "NWSA Distributable Revenue"). To allow for a comparison of financial results between years, the table below has been revised to capture 2014 actual and 2015 forecasted results under the new organization structure. Prior year revenues and expenses associated with properties licensed to the NWSA are labeled "Licensed NWSA Assets."

Please note that 2014 actuals and 2015 forecasted Licensed NWSA Assets operating revenues and expenses represent *gross* revenues and expenses associated with the Port of Seattle facilities that were licensed to the NWSA starting in 2015. For the 2016 budget, NWSA gross revenues and expenses are reported externally by the NWSA, not by each Port. The Port will instead recognize Distributable Revenues in 2016 equal to its (50%) share of the NWSA budgeted 2016 NOI. As such, the most meaningful comparison of NWSA financial results year over year would be at the NOI level.

TABLE X-3: FINANCIAL SUMMARY – NON-AIRPORT OPERATIONS (\$ millions)

	2014 Actual ⁽¹⁾	2015 Forecast ⁽¹⁾⁽²⁾	Final Budget
<i>Operating Revenues:</i>			
NWSA Distributable Revenue	\$ -	\$ -	\$ 51.8
Licensed NWSA Assets	68.4	65.2	-
Maritime Division	43.8	47.0	49.3
Economic Development Division	16.3	17.0	13.7
Other ⁽³⁾	0.4	3.0	3.9
Total Operating Revenues	\$ 128.9	\$ 132.2	\$ 118.8
<i>Operating Expenses:</i>			
Licensed NWSA Assets	\$ 22.8	\$ 23.4	\$ 0.1
Maritime Division	31.9	34.7	42.3
Economic Development Division	23.5	20.1	23.3
Other ⁽⁴⁾	0.4	0.3	2.1
Total Operating Expenses	\$ 78.6	\$ 78.4	\$ 67.8
Net Operating Income	\$ 50.2	\$ 53.8	\$ 51.0

(1) 2014 actual and 2015 forecasted results were restated to reflect organization structure effective in 2016.

(2) 2015 Forecasted figures are based on updates through Q3-2015.

(3) Consists primarily of Corporate operating revenues and those from Stormwater Utility operations.

(4) Consists primarily of unallocated Corporate operating expenses and those from Stormwater Utility operations.

The 2015 non-aviation NOI is forecasted to increase \$3.6 million relative to 2014. The increase is driven largely by a \$4.3 million increase in NOI (i.e. decreased net operating loss) from the Port's Economic Development division, which is primarily the result of decreased operating expenses in 2015. In 2014, the Port recorded a non-recurring litigation reserve for a lawsuit related to the Eastside Rail Corridor, which resulted in a (one-time) \$1.4 million hit to 2014 operating expenses. The forecasted Economic Development division NOI increase is partially offset by a \$3.8 million NOI decrease from the Port's container operations (i.e. Licensed NWSA Assets), which forecasts decreased 2015 operating revenues stemming from termination of the Terminal 5 lease in July 2014, and increased 2015 forecasted maintenance expense, particularly at Terminal 5, and corporate expenses related to the establishment of the NWSA. The Maritime division's forecasted 2015 NOI is slightly higher compared to 2014, with increased operating revenues associated with the cruise and grain business (cruise passengers and grain volumes were up 9.0% and 9.9%, respectively, year-to-date through October 2015) largely offset by increased maintenance expenses. Container volumes, measured by NWSA TEU's, are forecasted to increase 3%, from 3.43 million in 2014 to 3.53 million in 2015.

The 2016 non-aviation budgeted NOI reflects a decrease of \$2.8 million relative to the 2015 forecast. This is driven largely by decreased NOI budgeted for the Maritime and Economic Development divisions, partially offset by increased NOI for the NWSA. The \$5.2 million decrease in the Maritime division's NOI is driven primarily by increased budgeted allocated corporate expenses as well as other facility maintenance expense including new stormwater utility assessment expenses. These increases in operating expenses are partially offset by increased operating revenue associated with cruise and recreational marinas. The \$6.5 million decrease in the Economic Development division's budgeted NOI is driven

primarily by decreases in operating revenues from conference and event center operations, which will be impacted by large construction efforts at Pier 66 related to the expansion of the cruise passengers processing facility. The Economic Development division also budgeted increased allocated corporate operating expenses, in addition to increased operating expenses associated with the Office of Social Responsibility, Tourism, and Development and Planning, which reflect new and expanded Port initiatives. The decrease in 2016 budgeted NOI from the Maritime and Economic Development divisions is partially offset by \$9.9 million in increased NOI associated with the NWSA, which is the result primarily of decreased corporate allocated costs, and also some modest increases associated with the NWSA volume-based revenues at its container facilities. Container volumes are budgeted to increase an additional 2% in 2016.

For additional details about the Maritime and Economic Development division's operating budget and forecasts, please see Sections V, "Maritime" and VI, "Economic Development", respectively. Please refer to Section XII, "The Northwest Seaport Alliance 2016 Budget", for additional details on the NWSA operating forecast.

C. Overview of the Draft Plan of Finance

Each year the Port prepares the Draft Plan of Finance (the Plan) as part of the capital management process. The Plan provides a framework for the funding of the Port's anticipated capital spending, and is designed as a flexible tool, providing guidance to the Commission and Port staff as planning and investment decisions are made during the coming year. The Plan is based on a five-year capital plan in order to provide better guidance on long-term funding.

Once a year, the Commission is presented with the Port's capital plan along with a funding analysis. By final budget action, the Commission approves the capital plan and establishes the level of the Port's tax levy for the coming year. The first year of the capital plan forms the basis of the Port's approved Capital Budget. Each quarter capital spending forecasts are updated and progress is measured on spending versus budget; this is reviewed quarterly by each division and Senior Management and periodically by the Port Commission.

D. Overview of the Funded Capital Plan

The capital plan is the result of an iterative process that begins with business plan forecasts developed and approved by each operating division. The business plans, which contain operating and capital forecasts, are then reviewed in the context of the Port's projected capital capacity and further reviewed by Port Executive staff. The final business plan, including the capital plan, is incorporated into the Budget and into the Plan of Finance. For information on the Port's Capital Improvement Program (CIP), see Section IX "Capital Budget."

Within the capital plan, projects are divided into several categories that determine their funding priority.

- **Committed**: Committed projects are those necessary to implement the divisions' business plans and are well scoped, have undergone financial analysis and at least division level review. They include projects that are already underway and authorized as well as projects not yet authorized, but ready for Commission level review. These projects receive a specific funding commitment in the Capital Plan.
- **Prospective**: Prospective projects may also be part of business plans, but are not yet well-scoped and analyzed and therefore are less certain as to timing or funding requirements. Prospective projects can be re-classified as Committed once they have met the necessary criteria, so it is important that capital

funding be flexible enough to accommodate these projects as well as other changes to the CIP. Prospective projects are further subdivided into two categories as follows:

- Business Plan Prospective: Projects that are prospective because of uncertainty of scope and timing, but are deemed to be critical for achieving business plan goals. This category may include projects that are contingent obligations associated with leases or other agreements.
- Other Prospective: Projects that are still in preliminary planning or that are not currently deemed critical in meeting business plan goals.
- Public Expense Projects: In addition to the CIP, the Port participates in several public projects, particularly in the area of regional transportation and contributions to Highline School District noise mitigation. Because these projects do not result in Port owned assets, they are accounted for separately as Public Expense Projects, but they use the same funding as capital projects and are included in the funding analysis for the Plan of Finance.

Committed projects are designated for funding and are the basis of the Plan of Finance. This year's Plan of Finance also includes all Business Plan Prospective projects. The overall capital and funding approach for the 2016 Plan was divided into two major components, *Airport* and *Non-Airport*. The Airport is subject to certain regulatory restrictions, and as such, its capital plan is funded separately from the Non-Airport businesses. The Non-Airport business capital plans cover the newly formed Maritime and Economic Development divisions. The NWSA capital plan is not included in the Port's CIP, but the Port's funding of its share of the NWSA CIP is included in the draft Plan of Finance. Both the Airport and Non-Airport segments fund an allocated a portion of the Corporate division's capital.

As consistent with prior years, the 2016 Plan was developed to meet certain financial targets, including a minimum 1.8x debt service coverage on its First Lien Revenue bonds, 1.25x coverage on Airport revenue bond debt, and 1.5x coverage on Non-Airport revenue bond debt, minimum Airport operating fund balance equal to 10 months of operating and maintenance expenses (O&M) and a minimum Non-Airport operating fund balance equal to 6 months of O&M (for a Port-wide target of 9 months of O&M). The Plan is developed so that these targets are met in most years; temporary, minor dips below the targets can be tolerated if the Plan projects a rebound to meet at least the minimum targets.

Since 1991, the Port Commission has authorized its property tax levy below the maximum levy allowable, thus preserving the flexibility for the Port to increase the levy if needed. The Port levied \$75.9 million in both 2008 and 2009, and reduced the levy amount to \$73.5 million in 2010 and 2011. Beginning in 2012, the Port further reduced the levy amount to \$73.0 million through 2015, and has decreased the levy further to \$72.0 million in 2016. Consistent with policy, the Plan retains at least 25% of the tax levy for general purposes and uses no more than 75% for Limited Tax General Obligation (G.O.) bond debt service. This policy is more restrictive than the Port's statutory authority for G.O. bond debt. Based on statute, the Port estimates approximately \$750.8 million of remaining capacity of non-voted G.O. bond debt. For more tax levy information, see Section VIII "Tax Levy."

E. 2016-2020 Funding Plan

AIRPORT

The funding Plan for the Airport includes Airport net income, operating funds in excess of the minimum target fund balance, existing bond proceeds and future revenue bond proceeds. The Airport expects federal grant money for capital improvements for runway construction, noise mitigation, and security

related projects. Passenger Facility Charge (PFC) collections (net of PFC bond debt service and net of PFCs applied to pay existing revenue bond debt service) also provide capital funding. Customer Facility Charge (CFC) collections, net of the payment of operating and debt service costs associated with the Consolidated Rental Car Facility, may provide additional capital funding for future Consolidated Rental Car Facility upgrades and the acquisition of buses, as necessary. Additionally, the Plan anticipates the use of the tax levy to fund the portion of Highline School District noise improvements that are ineligible for Airport funding.

The current funding Plan includes all of the Airport's Committed and Business Plan Prospective projects, in addition to an allocated portion of the Corporate CIP. The Aviation division's committed capital plan consists of five major projects. First is the development of a new International Arrivals Facility for international passengers, which is needed to expand capacity to process the Airport's growing international passenger base. The second major project is the replacement and reconfiguration of the baggage screening equipment to improve operational efficiency and increase capacity. Third is the Port's NorthSTAR program that includes renovating and reconfiguring the North Satellite Terminal and certain main terminal facilities that connect to the North Satellite terminal. This effort will add additional gates, address seismic concerns, and upgrade HVAC, lighting and fixtures. The fourth major project is the reconstruction of Runway 16C/34C, which was largely completed in 2015 with taxiway improvements continuing into 2016 and 2017. The fifth is the renovation of the South Satellite that will ramp up near the end of this five year planning horizon. In addition to these major projects, there are several smaller renewal and replacement projects. For more details about the major capital projects, please see Section IX, "Capital Budget."

TABLE X-4: 2016-2020 AIRPORT CAPITAL PROJECTS FUNDING (\$ Millions)

Airport Funding Sources:

Net Income and Operating Funds	373
Existing Bond Proceeds	142
Passenger Facility Charges	248
Customer Facility Charges	2
Federal Grants	157
Tax Levy ⁽¹⁾	3
Future Revenue Bond Proceeds	1,160
Total Airport Funding Sources	<u>2,085</u>

Airport Capital:

Airport CIP (Committed and BPP)	2,050
Corporate CIP Allocated to Airport ⁽²⁾	35
Total Airport Funded Capital	<u>2,085</u>

⁽¹⁾ For capital spending only (portion of Highline School District improvements that are ineligible for Airport funding).

⁽²⁾ Assumes funding with Net Income only.

In addition to the above funding plan for capital projects, Aviation's 2016-2020 funding plan includes approximately \$3.8 million of expenditures for public expense projects (projects that meet the criteria of Committed or Business Plan Prospective projects but the expenditures are expensed instead of

capitalized). For more details about the Port's public expense projects and their funding, please see Section IX, "Capital Budget".

NON-AIRPORT

During 2015, the Port completed an internal reorganization of its Non-Airport businesses, which provided an opportunity to refine its capital funding approach. The funding approach for the 2016-2020 Plan consolidates all Non-Airport CIP (including CIP from the newly formed Maritime and Economic Development divisions along with the Port's contribution for its 50% share of the NWSA CIP) and allocates funding based on management guidelines. This is a diversion from the historical funding approach, which was segmented by specific division (formerly Seaport and Real Estate), with funding policies specific to each.

The 2016-2020 Plan funds all of the Committed and Business Plan Prospective projects for all Non-Airport CIP, in addition to an allocated portion of the Corporate CIP. Non-Airport funding includes net income, excess General Fund cash above minimum balance requirements, and federal grants for the Terminal 46 Modernization project under the Transportation Investment Generating Economic Recovery (TIGER) grants program. The Non-Airport funding Plan is based on the income projections associated with the Maritime and Economic Development divisions, and assumes 50% for the Ports share of the NWSA forecasted NOI. The Plan targets 1.5x debt service coverage on all Non-Airport revenue bond debt. The Plan also estimates approximately \$35.0 million of additional capacity beginning in 2019 that can be used for projects not yet in the capital plan.

The Maritime division CIP focuses on investments in facilities and infrastructure to support economic growth for cruise, the fishing industry, and recreational boating. The most significant Maritime capital projects include an expansion of the Pier 66 cruise passengers processing facility, in partnership with Norwegian Cruise Line Holdings, along with upgrades to Shilshole Bay Marina and Fishermen's Terminal. The Economic Development division CIP focuses on renewal and replacement of existing assets, primarily at Terminal 102, Pier 69, Pier 66 and the Bell Street Garage. More information on specific Maritime and Economic Development division projects can be found in Section IX, "Capital Budget".

Additionally, the Non-Airport capital plan also assumes 50% of the "open" and "capitalized" projects within the Northwest Seaport Alliance capital forecast. Open projects are on-going projects or projects ready to move forward that have customer commitment or a high degree of certainty. The determination of whether to capitalize or expense a project is driven by accounting rules, and any open projects that are deemed to be expensed are excluded from the NWSA CIP. These expense projects will reduce the NWSA NOI (and thus reduce the revenues received by each Port). Significant NWSA projects included in the Plan are the design and construction related to the Terminal 46 dock rehabilitation effort in the North Harbor (Seattle), along with the acquisition of container cranes and straddle carriers, pile cap and paving repairs and fender replacements in the South Harbor (Tacoma).

There are also projects forecasted by the NWSA that are not included in the CIP ("estimate"). These projects are based on an identified business need or opportunity, but have not been fully developed in scope and cost. These projects include the redevelopment of Terminal 5 in the North Harbor and Terminal 4 in the South Harbor. As part of developing the 2016-2020 Plan, the Port estimated its funding capacity for its estimated share of these projects at \$237 million using combination of tax levy, G.O. bonds and net income. The funding plan below does not include these projects.

More information on the NWSA capital forecast can be found in Section XII, "The Northwest Seaport Alliance 2016 Budget".

TABLE X-5: 2016-2020 NON-AIRPORT CAPITAL PROJECTS FUNDING (\$ Millions)

Non-Airport Funding Sources:

Net Income and Operating Funds	177
Grants	10
Tax Levy	50
Total Non-Airport Funding Sources	<u>237</u>

Non-Airport Capital:

Maritime Division	112
Economic Development Division	25
Northwest Seaport Alliance	59
Allocated Corporate CIP ⁽¹⁾	7
Additional Available Capacity	35
Total Non-Airport Funded Capital	<u>237</u>

(1) Assumes funding with Net Income and Operating Funds only.

In addition to the above funding for capital projects, the 2016-2020 Plan includes an estimated \$11.8 million of expenditures for certain freight mobility public expense projects, which meet the criteria of Committed or Business Plan Prospective projects but the expenditures are expensed instead of capitalized. For more details about the Port's public expense projects and their funding, please see Section VIII, "Tax Levy," and Section IX, "Capital Budget."

CORPORATE

The Corporate capital program is predominantly Information and Communication Technology (ICT) department projects associated with critical infrastructure and network security enhancements required to maintain compliance with established industry standards. A small portion of the CIP is for small capital equipment purchases and vehicle fleet replacement. Corporate capital costs are allocated to and funded by the operating divisions, as presented above in Tables X-4 and X-5. See Section IX, "Capital Budget," for additional information on Corporate CIP.

SR99 Tunnel

On February 9, 2010, the Commission approved a memorandum of agreement (the "MOU") with the Washington State Department of Transportation regarding the Port's participation in the replacement of the Alaskan Way Viaduct with a tunnel and on August 6, 2013, approved a funding agreement with the State. Under the original MOU, the Port's contribution was not to exceed \$300 million. Under the funding agreement, the Port was credited with \$19 million already contributed to a related freight mobility project (FAST Corridor) and agreed to contribute an additional \$267.7 million in two installments: \$120.0 million by May 1, 2015 and the remaining \$147.7 million by May 1, 2016. The agreement also included the potential for an additional \$6 million contribution by the Port at its discretion. The Port made the \$120.0 million installment payment in 2015, and expects to pay the remaining \$147.7 million commitment from a combination of bond funding (G.O. bonds to be issued in the future) and proceeds of the Tax Levy reserved in the Transportation and Infrastructure Fund. The Plan includes funding for this remaining \$147.7 million commitment.

FINANCIAL IMPLICATIONS AND RISKS

The funding Plans above include projects currently identified as Committed and Business Plan Prospective. The Plan meets the First Lien Revenue Bond coverage target of at least 1.80x coverage and results in First Lien coverage range between 4.72x and 5.89x. The Plans were also designed to meet the targets of Airport revenue bond coverage of 1.25x and Non-Airport coverage of 1.50x. The result is that (Port-wide) coverage for all revenue bond debt service (irrespective of lien) ranges from a low of 1.41x to a high of 1.55x (calculated assuming that a portion of Revenue Bond debt service is paid from PFCs and CFCs).

There are a number of risks that should be considered with regard to the above funding Plan. While the Committed projects are fairly certain, the Business Plan Prospective projects are still uncertain with regards to scope and timing; an increase in costs or acceleration of schedule for these projects could change the funding forecast. In addition, the Plan does not include Other Prospective projects, projects that are not currently contemplated but may be required for security, renewal and replacement or to address changes in the business environment, nor Estimate projects for the NWSA. In addition, the forecast is based on a number of assumptions related to operating income and tax levy collection; changes in these assumptions could affect the Plan results as well. To minimize coverage impacts, the Port could employ a number of options:

- delay or reduce project spending
- further reduce operating costs or identify additional revenues
- utilize alternative financing for appropriate projects
- seek additional grant funding
- increase airline rates and charges within the limitations of SLOA III
- increase the tax levy, subject to statutory constraints
- implement the Industrial Development District levy

Prior to implementation, these mechanisms would be further evaluated in the context of business planning, asset liability management goals and Port policy objectives. Given potential costs and/or risks associated with each, it is likely that the Port would pursue a balanced approach to minimizing coverage impacts, whereby it would utilize a combination of options.

The Plan of Finance assumes a levy amount of \$72.0 million in 2016-2020, which is below the Port's actual statutory authority of \$96.4 million in 2016. The Port can access additional funding sources including remaining non-voted G.O. bond capacity and voted G.O. bond capacity, assess the tax levy up to the maximum amount or assess an Industrial Development District (IDD) levy (subject to limitations described in Section VIII "Tax Levy"). There are no plans to use these resources at present, but they are available should the Port Commission deem them appropriate.

F. Financing Initiatives

In April 2015, the Port issued \$157.0 million of 2015 G.O. and Refunding Bonds. The bonds were issued to fund the Port's first installment owed to the Washington State Department of Transportation related to the SR99 Deep Bore Tunnel Project, as described above, and to refund the outstanding 2006 G.O. bonds maturing in 2016 and beyond. The refunding transaction resulted in net present value savings of approximately \$11.0 million.

In August 2015, the Port issued \$582.7 million of 2015ABC Intermediate Lien Revenue and Refunding bonds. \$298.3 million was issued to fund new Aviation capital projects, and \$284.4 million was issued to

fully refund the outstanding 2005A Intermediate Lien Revenue Bonds. The refunding transaction resulted in net present value savings of approximately \$42.3 million.

In November 2015, the Port replaced an existing letter of credit backing \$150 million of Subordinate Lien Revenue Notes (Commercial Paper) with a new \$125 million letter of credit that expires in 2020. The existing letter of credit expired in November 2015.

In 2016, the Port expects to issue G.O. bonds to fund the second and final installment owed to the Washington State Department of Transportation related to the SR99 Deep Bore Tunnel Project. Additionally, in light of the continued low interest rate environment, the Port will continue to monitor the debt portfolio for refunding opportunities that provide for economic savings. The Port will also evaluate options of extending and/or replacing three existing letters of credit on variable rate debt, which are scheduled to expire in 2016.

G. Capital Planning Resources

The following information on funding guidelines and financial model assumptions are resources for better understanding the 2016 Draft Plan of Finance.

PORT OF SEATTLE FUNDING GUIDELINES

The following guidelines have been prepared to assist the Commission, Port management, and staff in decisions regarding the allocation of Port capital funds.

Tax Levy and General Obligation Bonds

Section VIII, "Tax Levy," describes the various uses of the tax levy including the funding of certain capital projects. Generally, the Port has used the tax levy for environmental remediation, regional transportation projects, and for certain capital expenditures that met the following criteria:

- A long lag exists between capital costs and project revenues or the project's financial return will not support revenue bond financings (i.e. the internal rate of return, or IRR, is less than the current cost of debt); and
- The project generates significant economic benefits for taxpayers.

To further assist in determining which projects to fund with the tax levy, the following matrix was developed:

	<u>Fund from Operating Income</u>	<u>Eligible for Tax Levy Funding</u>
Asset Renewal and Replacement	Supports an operation that generates positive net income	Supports an economic benefit operation
Investment in a Strategic Initiative	Investment has a short payback period/ is self-funding	Investment has no or a long payback
Location of the Asset	South Harbor	North Harbor

Based on these criteria, the 2016 Plan assumes the tax levy funds renewal and replacement projects of assets that support the fishing industry as well as a strategic investment in the Pier 66 cruise terminal.

In addition to funding capital projects, G.O. bonds may be used for public expense projects in addition to capital projects. For large public expense items this provides for more prudent cash flow management by

spreading out payments over time. Similar to capital projects, public expense projects are expected to meet the criteria noted above to be eligible for tax levy or G.O. bond funding.

Revenue Bonds

Projects should earn the current cost of debt (in IRR terms) or otherwise be included in the airlines' rate base to be eligible for revenue bond financing. A target senior lien revenue bond coverage ratio of 1.8x will be reviewed annually in light of changing circumstances such as critical funding needs or changes in the airport-airline operating agreement. An adequate cash flow margin (cash flow after debt service) will also be maintained for planning purposes.

Industrial Development District (IDD) Levy

In order to be considered for IDD levy financing, projects should be critical to core Port business or other major strategic initiatives, and should generate significant economic benefits for taxpayers. Additionally, projects must comply with all applicable legal requirements governing the use of the levy.

Airport Improvement Program (AIP) Grants and Passenger Facility Charges (PFCs)

Projects eligible for AIP grant and PFC funding should be consistent with airport investment strategies and must comply with the regulations of the grant-making agency. High priority safety, security and capacity projects will be stressed.

Funding vs. Asset Life

Project funding should in all cases closely match the life of the particular asset financed. For example, long-term financing in the form of 20-30 year revenue or G.O. bonds should only be used for assets having economic lives in a similar range or longer. Shorter-lived assets should be funded through pay-as-you-go or other short-term financing structures.

2016 DRAFT PLAN OF FINANCE ASSUMPTIONS

Capital Budget

Capital budget projections are aligned with the capital presentations provided to the Port Commission in October 2015, and are included in Section IX "Capital Budget."

Capital Capacity Calculations

The Port's capital capacity calculations combine projections of operating revenues, expenses, non-operating items, debt service, and capital spending to determine Port debt financing requirements. Assumptions used in the financial analysis of the 2016 Plan include:

- Interest earned on restricted and unrestricted funds based on 1.0% interest rate in 2016, and 1.50% from 2017-2020.
- New G.O. bonds are issued at 6.0% for 25 years.
- New First Lien revenue bonds are issued at 6.0% for 25 years. Not applicable in 2016-2020 time period.
- New Intermediate Lien revenue bonds are issued at 6.0% for 25 years. Intermediate Lien is the assumed working lien for new Airport debt.
- 1% gross up assumed for all new debt to account for Cost of Issuance.
- 8% and 9% gross up assumed for the Debt Service Reserve Fund contribution (cash funded) for new Aviation and Non-airport revenue bond debt, respectively. No new Non-airport debt assumed in 2016-2020 time period.

- Gross up for new Aviation debt of 18 months of Capitalized Interest.
- Interest on variable rate bonds (issued in 1997 and 2008) is based on projections of short and long-term tax-exempt variable rates and range from 1.10% to 3.00%.
- 2016 operating revenue and expense forecasts are based on the 2016 preliminary operating budget as of November 2015, with adjustments as appropriate, and may vary from the forecasts in the 2016 final budget.

Tax Levy

The Port's tax levy projections are based on maintaining the levy amount at \$72.0 million.

A tax levy projection model is used to forecast future year assessed value amounts that can affect the maximum statutory levy.

Revenue and Expense Assumptions

Airport

- Expense projections are based on estimates developed as part of division business planning.
- Airport aeronautical revenues are determined according to the 2013 airline agreement (SLOA III). SLOA III establishes several types of fees designed to recover operating and capital costs of the associated aeronautical facilities on the Airfield and in the Air Terminal. The Airfield is comprised of three areas: the Airfield Apron Area, the Airfield Movement Area and the Airfield Commercial Area, and related costs and fees are calculated separately for each area. Terminal rental rates are based in part on the Terminal Building Requirement, which is computed by multiplying the total of budgeted operating expenses and capital costs, including debt service and debt service coverage (if required), allocated to the terminal, by the ratio of airline rentable space to total rentable space, less any non-signatory airline premiums included in rent payable by non-signatory airlines. Excluded from the cost recovery formula is any airline office or club space that is vacant. SLOA III provides for the sharing of a portion (50%) of Airport net revenues if Airport debt service coverage exceeds 1.25 times. SLOA III expires December 31, 2017, but is the basis of the aeronautical forecast for the entire five-year period.
- Airport non-aeronautical revenues are based on forecasted passenger growth and the revenue terms of current leases and agreements associated with non-aeronautical businesses.
- Operating environmental costs are included in O&M expense.
- Certain non-operating revenues and expenses are included; for example, interest earnings, debt-related fees, public expense items and non-operating environmental expenses.
- Federal Airport Improvement Program (AIP) grant reimbursement projects are based on estimated spending on eligible projects and standard reimbursement rates of 75%-80%. Grants from the Transportation Security Administration (TSA) are included in the total grant amounts.
- Passenger Facility Charges (PFCs) are estimated based on projected enplanement levels, net of debt service payments on PFC bonds and PFCs applied to pay debt service on Revenue Bonds.
- Customer Facility Charges (CFCs) are estimated based on forecasted transaction days of car rentals at the Airport multiplied by a forecasted daily rate. The 2009 First Lien Revenue Bonds and Commercial Paper proceeds along with any CFC income (net of debt service) are expected to fund any remaining Consolidated Rental Car Facility capital projects.

Non-Airport

- Revenue and expense projections are based on the Maritime and Economic Development division's long-range operating forecasts, which are based on the terms of existing lease agreements and projected activity levels for any applicable volume based revenues. Revenues generated from new investments were not included. The Port also assumed 50% of the forecasted NWSA NOI as operating revenue.
- Estimated security grant receipts for operating grants are included in gross revenues and the associated expenditures are included in operating expenses, if applicable.
- Operating environmental costs are included in O&M expense, if applicable.
- Certain non-operating revenues and expenses are included; for example, interest earnings, payment of public expense and other non-operating environmental expenses.

Corporate

Expenses for Corporate, including the former Capital Development division, are distributed to the operating divisions as corporate overhead.