

## Introduction

I strongly believe this board is well-prepared to do a rigorous, fair and independent evaluation of the detailed proposals that will be submitted in the next few weeks. What may be most important here is that this board is focused on finding what is best for the port and ultimately the Commonwealth. Of equal importance is the fact that we have and will continue to approach this task with open minds, which is inherent in our fiduciary responsibility as it relates to our work here.

- Collectively, we agree the evaluation process must be transparent and provide ample opportunities for public input. Before the board considers a position, it wants to ensure the port's stakeholders are heard and that their feedback is part of the evaluation process.
- The board is getting weekly reports from a working group that is evaluating the proposals; two members of that group are VPA executives.
- We have engaged a leading global consultant to help evaluate the current port operation and we see this as one of the most critical parts of our review. We are asking: Does the existing operation need to be refined, or will a new operator provide advantages that we cannot achieve under the current structure?
- Though a schedule exists, the board is committed to taking the necessary time to conduct a thorough review of the proposals with help from outside sources. In doing so we hope to minimize any uncertainty and show all interested parties that we will not be rushed into making a decision.
- My colleagues are experienced in all facets of business and were asked by the governor to serve on this board because of their business acumen, diversity and collective business experience. All of these qualities have been tested during this last year as we undertook a thorough review of port operations and the VPA/VIT relationship.
- In that review 1) we identified \$8 million in savings without jeopardizing service; 2) we authorized refinancing a portion of VPA bonds, with a savings of \$13.4 million; and 3) we made other personnel changes that will result in an annual savings of \$2 million. We have also started an evaluation of organizational finances and structures, which will help identify other critical areas where cost savings can be achieved.
- Though we have made progress, there is still much work to do. The opportunity we now have before us should enable the Port of Virginia to become stronger and more competitive than ever. Through evaluating these proposals, we will determine whether our efforts to grow the port and address the challenges we face are better served through our existing financing structure and operational model or if an alternative model will provide more opportunity.

## History

In the late 1960s, Gov. Mills Godwin established a port study commission in order to determine changes necessary to make Virginia's ports competitive. The recommendation was that Virginia Port Authority (VPA) be reorganized and that the state through the VPA, assume the ownership of the three marine terminals in Hampton Roads, thereby ending cutthroat competition among the terminal operators. Following this recommendation the process, which has since come to be known as Port Unification, began. Unification culminated in July 1972 when the VPA acquired the interest of the City of Norfolk in Norfolk International Terminals. The VPA had acquired Portsmouth Marine Terminal in July 1971 and Newport News Marine Terminal in October 1971.

- Having acquired each terminal, the commission recommended the VPA create a method to centrally operate all of the marine terminals. Thus a non-stock, non-profit corporation known as Virginia International Terminals, Inc. (VIT) was created to take over the operation of all three marine terminals. VIT commenced operation on Jan. 1, 1982.
- This structure was chosen in order to allow a private company to operate in a business environment and to negotiate with port labor unions in order to service ships and move cargo within the terminal. Virtually all East and Gulf coast ports are subject to a master collective bargaining contract with the International Longshoreman's Association AFL-CIO (ILA). The state however, then and now, is prohibited by Senate Joint Resolution 12 from dealing with organized labor and this continues to be a barrier against the State's direct operation of the terminals.
- As with the three individual operators, all of VIT's revenues were dedicated to either operating purposes or turned back to the terminal facilities for equipment purchases, maintenance and capital improvements.
- The consolidation of port operations under the management of VIT, in addition to resolving labor relation issues, enabled the terminals to engage in serious competition with other Mid-Atlantic ports seeking a role in the ever growing intermodal industry.
- The relationship between VIT and VPA is decidedly "arm's length." It has always been controlled by a Service Agreement detailing the responsibilities of each organization. The VIT Board of Directors, in accordance with its Articles of Incorporation, was originally composed of seven individuals appointed by the VPA board.
- In November 2011, the VPA board approved an amended and Restated Articles of Incorporation of Virginia International Terminals to add two VPA board members to the VIT board, thereby increasing membership to nine directors. By expanding the VIT board to include two VPA board members, it would provide a direct line of communication and enhance VIT's board with the talent from the VPA Board.

- VIT's revenues, after the payment of terminal operating expenses and overhead, are applied to support VPA bond issues periodically issued to purchase needed capital improvements and to support the revenue requirements of the VPA. As a result, the State's marine facilities support almost entirely the day-to-day operations of the VPA, including marketing the port throughout the world while at the same time funding the day-to-day operation of the terminals themselves.
- While the VPA exercises budget oversight as to terminal operations, VIT exercises independent control over its revenues and expenditures. Its bank accounts, insurances, purchases, employee relations and compensation and budget programs are all independently managed by VIT's administration. Contractual relationships, labor negotiations and ultimate fiscal decision-making are in the hands of VIT's management, which reports monthly to its board.

### **Benefits & Shortcomings**

- One of the biggest benefits of privatization could be the expansion of our overall competitiveness. With representation in the international market by a worldwide player, and their ability to draw upon worldwide best operating practices, Virginia could benefit from business opportunities that to this point have gone unrealized.
- Another benefit would be an overall reduction in financial risk, but this argument has two sides: Is it better to take the "sure" or guaranteed money on an annual basis and insulate ourselves from any risk? Or, do we manage ourselves and our risk better to make it easier to weather depressed economic periods and prosper greater during economic upswings?
- There is a potential for upfront proceeds.
- A shortcoming of privatization is that we take a portion of the decision-making process regarding strategic planning and terminal operations away from VPA and Virginia and leave that up to a new terminal operator.
- A loss of accountability from the terminal operator if the proper metrics aren't in place.
- A residual of privatization may be loss of jobs to both the current operating company (VIT) and with those vendors that do business with VIT. Vendors may also lose revenues, but it is far too early to say what either of these potential losses would look like.
- A 48-year-long operating concession would take us through 2061. The VIT Service Agreement can be cancelled at any time with 30 days notice.

## **Performance**

- The Port of Virginia did not weather the economic downturn as well as other US East Coast Ports and it has not bounced back as quickly. That said, port has been posting a very solid performance thus far in 2012 with an 8 percent increase in TEU volumes, year-to-date.
- As the economic downturn took hold, the port was not as aggressive as it needed to be at examining its internal operating structure to eliminate duplication between VPA and VIT as a means of reducing costs.
- The port's rail business continues to be its fastest growing area of business. CSX came on line this year and has created legitimate competition in the marketplace as a result. Total rail units up 15% through Aug.
- This year the port added a rail service to Greensboro, NC – the Piedmont-Triad region – and as a result has recaptured a market that was served primarily by trucks from the port in Charleston, SC.
- There is consideration of expanding our reach into western North Carolina with rail service to Charlotte, and other points west, as part of a larger effort to expand our overall market share vs. other USEC ports.
- A third sailing was added to the 64 Express barge service connecting the Hampton Roads Harbor and the Port of Richmond. Barge movements are up 105% through Aug.
- We are doing a better job at coordinating marketing efforts with partners at the Virginia Economic Development Partnership and are committed to continue through a recently-signed memorandum of understanding.

## **Challenges for the VPA Board**

- Clear all procedural hurdles to allow the board to operate without any ambiguity (as to its role).
- To remain neutral throughout the process while maintaining our fiduciary responsibility.
- Keep the process as transparent as possible while engaging the public on a regular basis.
- Ability to digest detailed evaluation of proposals, pick a preferred bidder and begin negotiations within a very aggressive timeline.

- Continue to leverage the assets of the port to push expansion as this process goes forward.
- Consider a reorganization plan to better align the VPA/VIT relationship while reducing duplication of services within the two organizations.
- In addition to reviewing the proposals, the board believes the evaluation of the existing operational model should be a part of the process.

### **Role of the Board**

The evaluation of these proposals requires a careful balancing act to ensure the best outcome is obtained. On one hand, the board understands that changing port operators and operating structure are serious decisions with long-term ramifications for the Commonwealth and the Hampton Roads maritime community that requires careful due diligence. On the other, we understand the uncertainty of the review process is not optimal, and that the board should act expeditiously to bring closure to the evaluation so that the focus is on building long-term competitiveness of the port.

As this review continues the board is asking tough questions about all aspects of this port. Specifically, can we do better? It's the right question to ask as we seek to position Virginia to attract more cargo by leveraging the host of unparalleled manmade and natural assets this port has at our disposal.