

THE NORTHWEST SEAPORT ALLIANCE
MEMORANDUM

MANAGING MEMBERS
ACTION ITEM

Item No. 9C
Date of Meeting April 4, 2023

DATE: March 24, 2023

TO: Managing Members

FROM: John Wolfe, CEO

Sponsor: Tong Zhu, Chief Commercial & Strategy Officer

Project Manager: Steve Balaski, Director of Business Development

SUBJECT: **The 2023 Northwest Seaport Alliance (NWSA) Rail Cargo Incentive Program**

A. ACTION REQUESTED

Request Managing Members of The Northwest Seaport Alliance (NWSA) authorization to fund a Rail Cargo Incentive Program at an initial level of \$3,000,000 and authorize the CEO to execute Participating Carrier Agreements for the program as presented. The rail incentive fund will include \$1,500,000 of NWSA cash plus \$1,500,000 of credit associated with Tacoma Rail for rental of the South Intermodal Yard.

B. SYNOPSIS

Approximately half the import cargo that comes through the NWSA is bound for destinations outside of the Puget Sound region (primarily the Midwest). Rail shipments remain a key driver of volume growth for the NWSA. The discretionary nature of this cargo means it will most often move via the lowest cost and most efficient option. Ensuring the NWSA is the most efficient and cost-effective gateway for both importers and ocean carriers is critical as the competitive nature of our industry continues to intensify.

Additionally, supporting the establishment and growth of inland rail hubs to drive agriculture export cargo to the NWSA remains a strategic initiative. This initiative has yielded the successful launch of several projects while others are in various stages of development. Due to the low-margin nature of agricultural exports, cost is the key

factor in routing decisions. A rail incentive can both encourage the growth of recently established operations and support the start of new service locations.

Based on the success of prior rail incentive programs, feedback from our ocean carrier customers and current market conditions, the 2023 rail cargo incentive program is expected to help protect NWSA rail market share in a down market and encourage incremental increase in rail volumes through the gateway.

In October 2020, the Managing Members approved a lease agreement with Tacoma Rail that allows the NWSA to incentivize rail cargo activity in the Tacoma Harbor and/or fund projects involving rail-related infrastructure improvements in the Tacoma Harbor in lieu of paying rent for the SIM. The accumulated rent credit can only be used to incentivize rail cargo in the South harbor. Some funds will be used to repair rail in the tideflats, resulting in a current amount available for incentives of approximately \$350,000. The amount available grows by approximately \$90,000 per month, and will total over \$1,500,000 by April 2024.

C. BACKGROUND

Import volumes at the NWSA and most West Coast ports are down due to a very soft Trans-pacific market. As the U.S. has emerged from the pandemic, consumer demand for key import commodities has declined. New purchase orders by major import shippers have been reduced, delayed or canceled as they work through continued elevated inventory levels while operating in a high interest-rate environment. As a result, ocean freight rate levels have seen a rapid decline from historic highs and are now at pre-pandemic levels. Ocean carriers are focused on cost-control as they forecast a challenging operating environment in 2023.

Given these market conditions and the operating priorities of our ocean carrier partners, the proposed rail cargo incentive program is an important tool to help protect market share and attract incremental volume to the gateway.

Staff has reviewed prior rail incentive programs to determine which elements were most effective and is recommending a program as follows:

- Eligible volumes must be incremental, measured on aggregate rail volumes of an ocean carrier at the NWSA.
- Eligible inland ramp locations will include all intermodal inland ramp locations served and/or operated by the BNSF and Union Pacific Railroads with the exception of Portland, OR. To support the NWSA's inland rail hub strategic initiative, ramp locations in Minot, ND, Pocatello, ID, Millersburg OR and Wallula, WA have been called out specifically as eligible for the program.

- Eligible rail volumes will receive a \$50/lift incentive.
- The suggested term of the program is May 1, 2023 through April 30, 2024.
- Ocean carriers must be **current** on their accounts with the NWSA to be eligible for the program. For purposes of this agreement, a carrier is deemed to be not current in its accounts if it has any accounts with NWSA over 30 days past due on the date that the NWSA makes the incentive payments. If a carrier is not current on the date incentive payments are made, the carrier will not be issued an incentive payment and will have 30 days to become current on all accounts in order to be eligible for the incentive payment or otherwise forfeit the incentive payment.
- Staff proposes a six-month measurement and payout period unless a shorter timeline is agreed to, at the discretion and approval of the NWSA CEO.

Volumes moving through both the North and South harbors would be eligible for the program. Given the requirement to apply the Tacoma Rail rent savings to cargo moving via South Harbor facilities, we are seeking additional funds from Managing Members to ensure the entire gateway can benefit from this proposed rail incentive program.

The need to offer the incentive plan for a full year has been a strong and consistent message from the ocean carriers. They have called out the lengthy and cumbersome challenges of changing cargo routings, only to see prior incentive plans terminate after a couple months.

Depending on the degree of success, additional funding beyond the original \$3,000,000 request may be required in order to administer the program for the full twelve months. Staff will provide a mid-year update and advise if a request for additional funding will be required.

Assuming total funds requested are distributed, we expect the incentive program to generate approximately 60,000 additional rail lifts, equivalent to approximately 15% of 2022 NWSA international intermodal lifts or 10% of the average of international intermodal lifts from 2019 – 2021.

D. FINANCIAL IMPLICATIONS

The \$3,000,000 rail incentive fund will include \$1,500,000 of NWSA cash plus \$1,500,000 of credit associated with Tacoma Rail for rent payments used for incentive vs rent payment of the South Intermodal Yard (SIM).

Per Lease Amendment No. 3 with Tacoma Rail (TMBL), the alliance has elected the lower rent option and use the savings in rent at the SIM Yard to fund rail incentives or maintenance of rail related infrastructure improvements in the South Harbor. The rail incentive is not budgeted in 2023. The 2024 operating budget will include any expected incremental rail incentive revenue and expenses. The impact to revenue is estimated to be \$1.0 million to \$1.3 million on a 12-month basis based on 2022 intermodal lifts by terminal, and accounting for the Minimum Annual Guarantees. The actual amount will vary depending on actual usage of the rail incentive by the ocean carriers.

E. ATTACHMENTS TO THIS REQUEST

- The 2023 NWSA Rail Cargo Incentive Program Description
- The 2023 NWSA Rail Cargo Incentive Program Agreement (example)