

Airport and Airline Use and Lease Agreements

Capital Program Control & Consultation,
Leasing Policies & Space Management,
and Rates & Charges Approaches

ACI-NA Airport Economics and Finance Conference
General Session II

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Introduction

- At a majority of US airports Airport-Airline Use Agreements form the basis for the business model for the financial operations and space management at US Airports.
- A wide range of approaches used at various airports – what is right for your airport will depend on the objectives of and circumstance at your airport.
- Airport and airlines may “occasionally” have differing perspectives on what is the optimal approach as well.
- During this panel we are going to explore some of pros and cons the different approaches taken by airports in three focal areas, as viewed by some airports that have recently negotiated new agreements, airline representatives, an airport consultant who has negotiated a number of airline agreements.

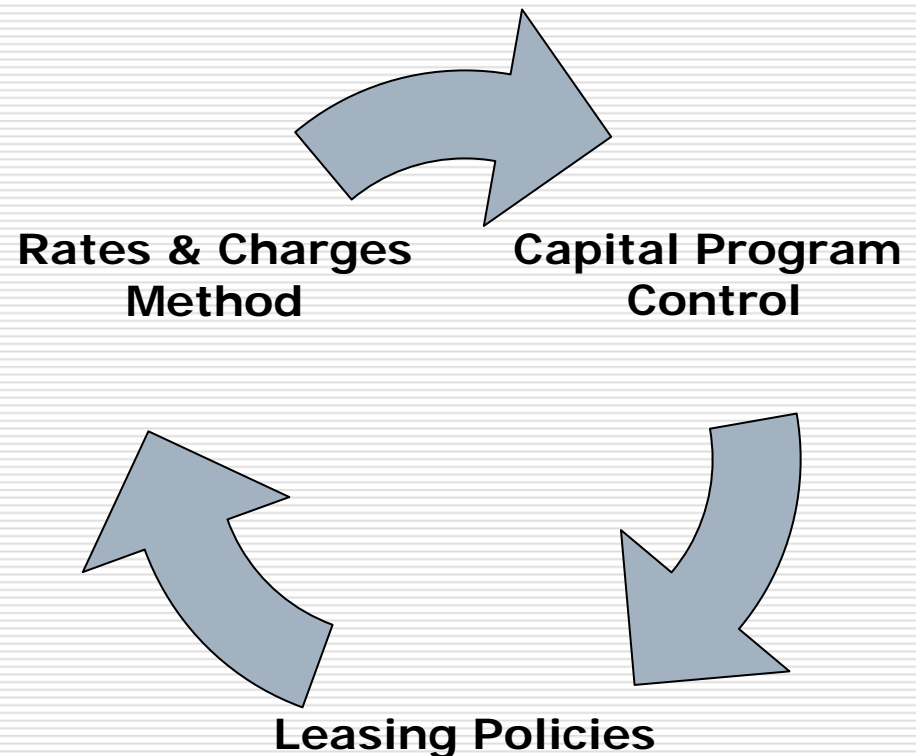
Panel

- ❑ Susan Warner-Dooley, Deputy Executive Director, Finance & Administration, Minneapolis-St. Paul Metropolitan Airports Commission
- ❑ Vince Granato, General Manager, Financial Services, Portland International Airport
- ❑ Luis Navarro, Manager-Aviation Properties, Seattle-Tacoma International Airport
- ❑ R. Borgan Anderson, Manager, Aviation Finance and Budget, Seattle-Tacoma International Airport
- ❑ Trey Hettinger, Airport Properties Representative, United Parcel Service
- ❑ Steve Sisneros, Regional Director, Southwest Airlines
- ❑ Warren Adams, Director, Jacobs Consultancy

Format for the Session

- **Three Areas of Focus:**
 - Capital program control and consultation processes
 - Leasing policy/space management
 - Rates & charges methodologies

- **Process For Each Topic:**
 - Overview
 - Airport Approach
 - Airline Perspective
 - Q&A



Construction Control & Consultation

Airline Involvement in Capital Project Decision Making

- Degree of Airline Involvement
 - Approve
 - Disapprove (deemed approved unless airline expressly disapproves)
 - Deferral
 - Consult Only

- Areas Of The Airport That Are Covered
 - Airfield
 - Terminal
 - Landside & Other

Trends: Capital Project Pre-Approval and Exemptions

- Approved Programs and Thresholds
 - Total Budget vs Approved List of Projects
 - Discretionary Projects

- Typical Exclusions
 - Safety, security, judgments, replacement ...

- Emerging Trends/Concepts in Exclusions
 - Capacity-Enhancing Additional Passenger Terminal Improvement Project / space for new or expanding carrier
 - Expenditures for Planning & Preliminary Design

- Potential New Exclusion
 - AIP or PFC funded projects at certain funding levels

Capital Consultation Q&A

Leasing Policies and Space Management

Leasing Approach

□ Trends

- Trend away from historical standard of exclusive gates to preferential, common use, or combination
- Shorter term airline agreements allow airlines to “resize” more frequently and to allow airport to reevaluate the use of their space

□ Issues

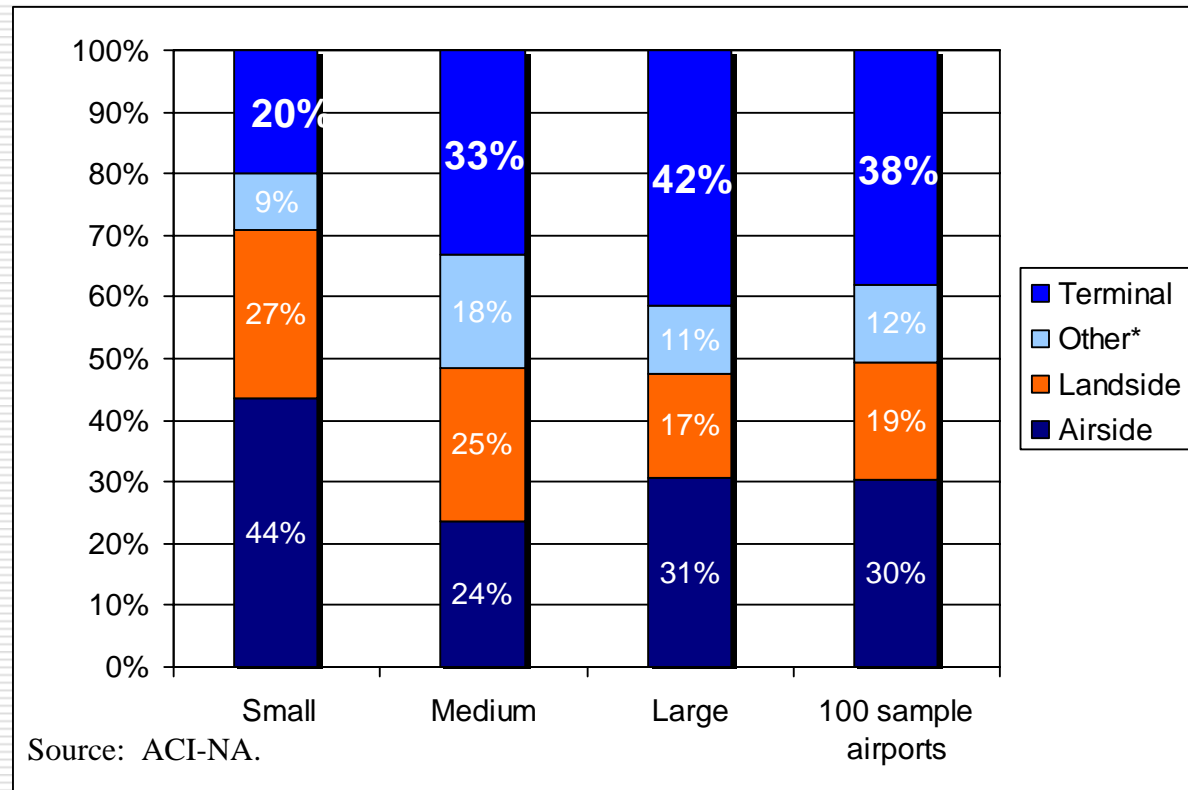
- Common Use Terminal Equipment (CUTE)
- Vacancy risk for airport operators may be increasing

□ New Approaches

- Formulas or changing ratio of preferential & common gates
- Different gate use ratios based on number of gates leased
- Link gate use to airline approval of new gates
- Shift of financial risks of vacancies to airlines

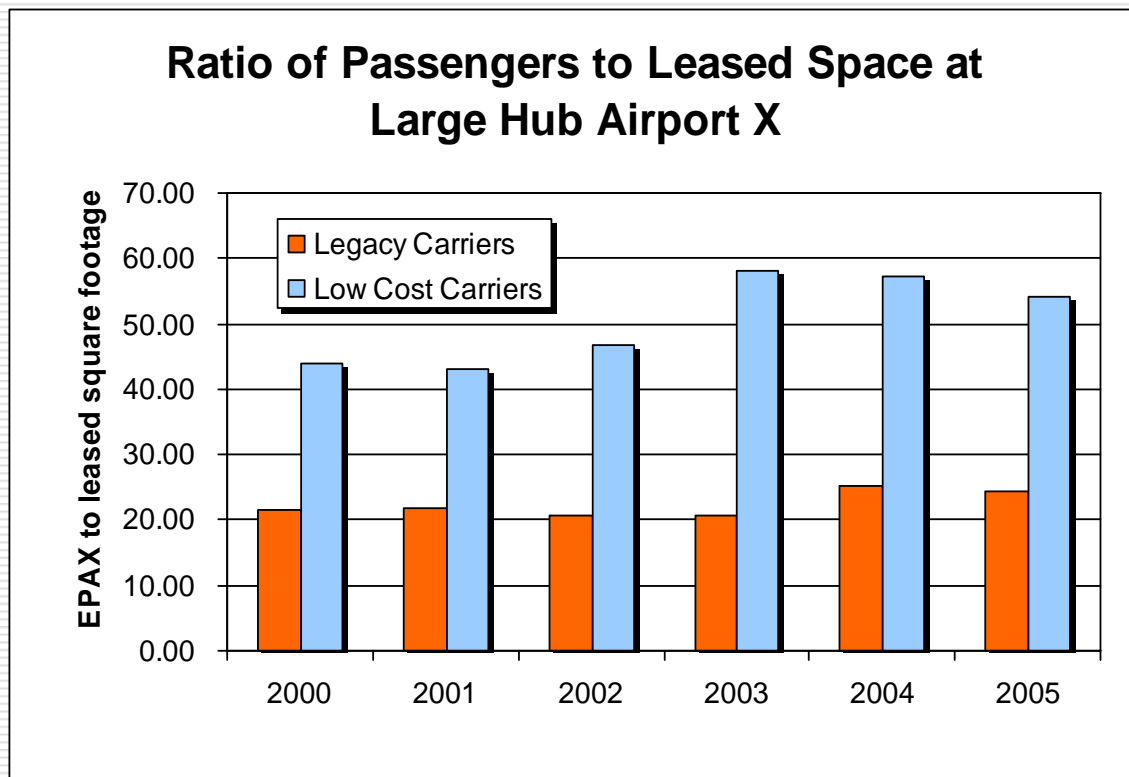
Terminal Buildings—The Next Big Investment

- About 40% of future capital needs focused on terminal facilities
- Challenges with terminal projects
 - Lack of “institutional” criteria for proceeding
 - Limited sources of “non-rate based” capital
 - Vacancy risk
 - Changing mix of airline usage



Leased Space: No Airport Control

- Low cost carriers are twice as efficient as legacy carriers in use of terminal space
- Near-term issue: **More vacancy risk in terminal**
- Ongoing risk: **Constant airline restructuring**



Note: A higher bar means more passengers per leased square foot of space.

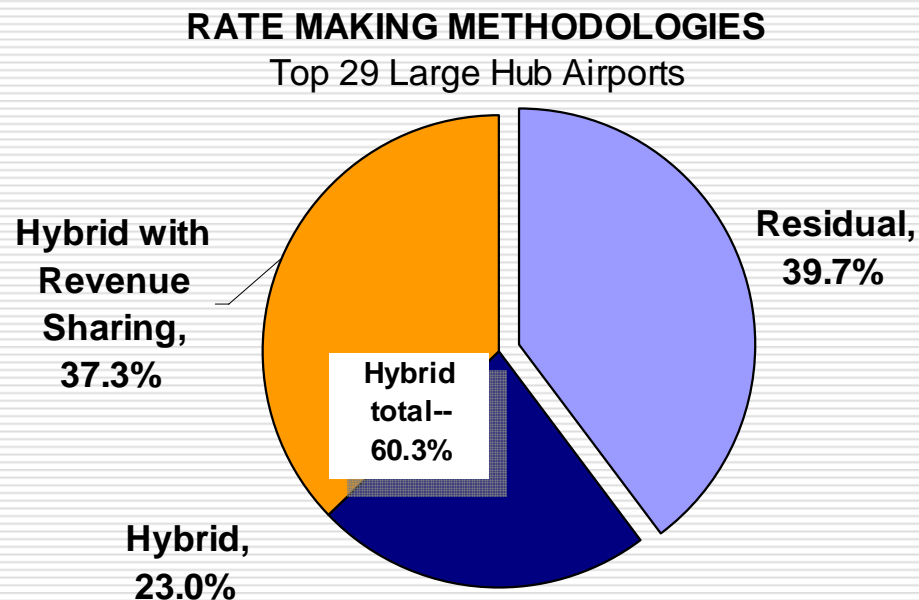
Space Management Q&A

Rates & Charges

Industry Snapshot: Rate Making Methodologies

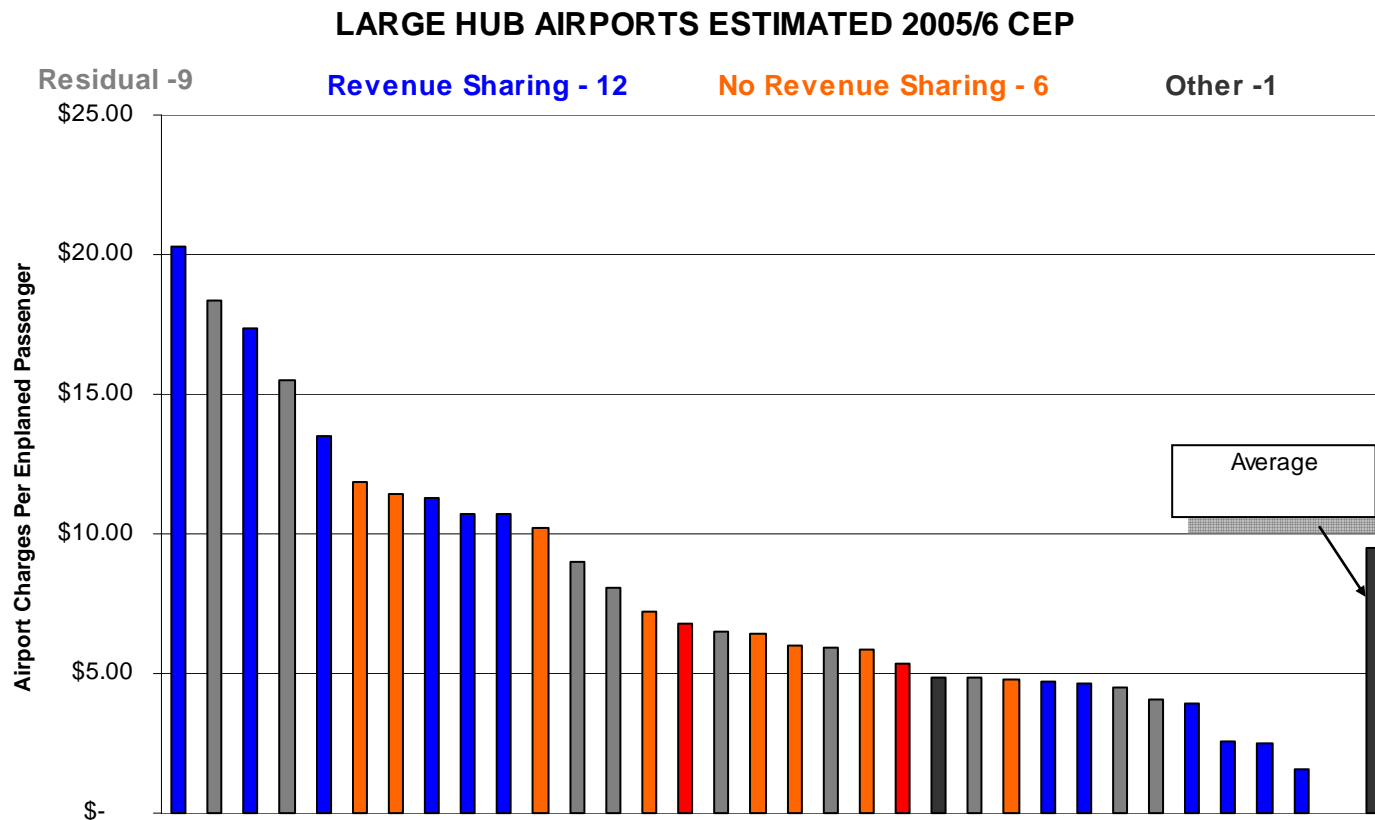
- Broad Categories of Residual, Compensatory & Hybrid
 - There is no defined or standard approach structure within the categories

- The use of a particular rate-making approach is typically integrally linked to other negotiated factors, such as
 - Facility use
 - Airline consultation or MII



Percent of total based on passengers. Hybrid includes the use of compensatory and residual rate-making methodologies. Results do not include HNL.

Rate Making Methodology and Level of Cost Per Enplaned Passenger—No Clear Link



Rate & Charges Components

- Getting to the Bottom Line
 - Airport Discretionary Funds or Accumulated Surpluses

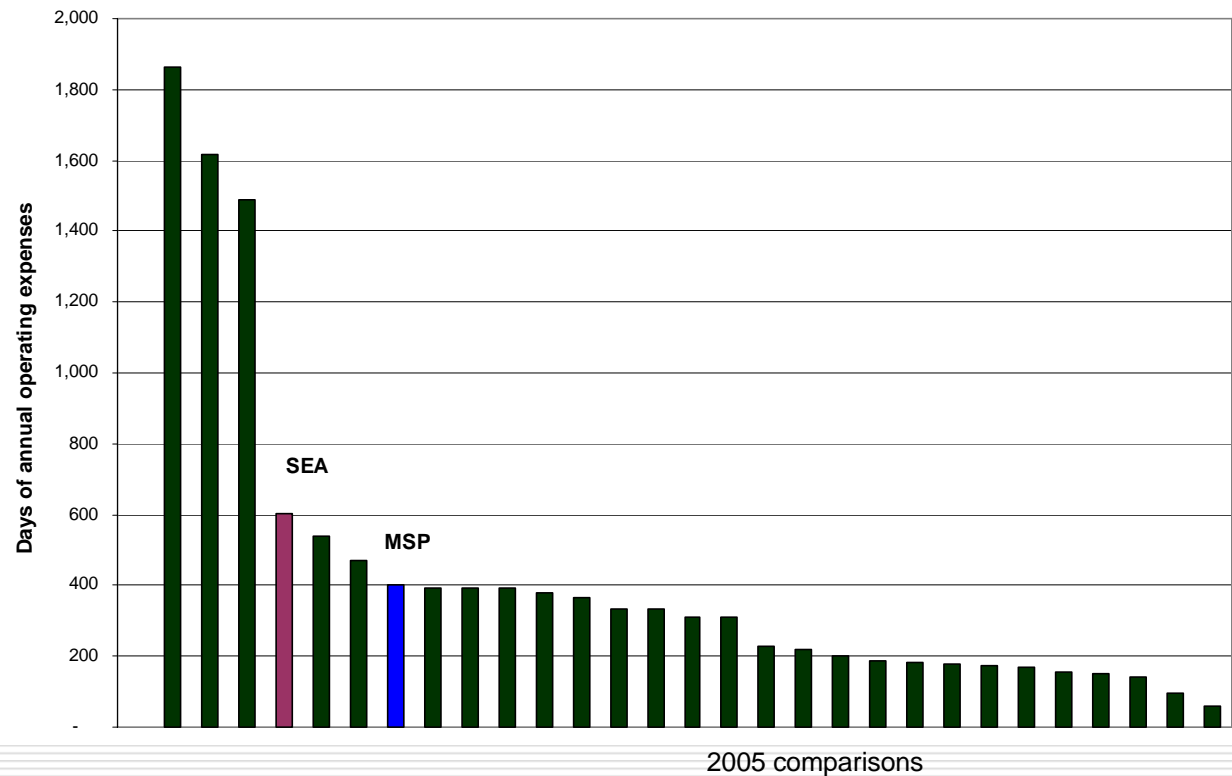
- Allocation of Risks/ Sharing of Revenues
 - Cost Allocations and Recoveries
 - Revenue Sharing
 - Bottom Line Protections

Discretionary Funds and Accumulation of Surpluses: Taking Rating Agency Metrics into Account

Best Practices

- Link airline deal with key rating agency metrics
- Establish airport goals regarding RA metrics to frame business deal

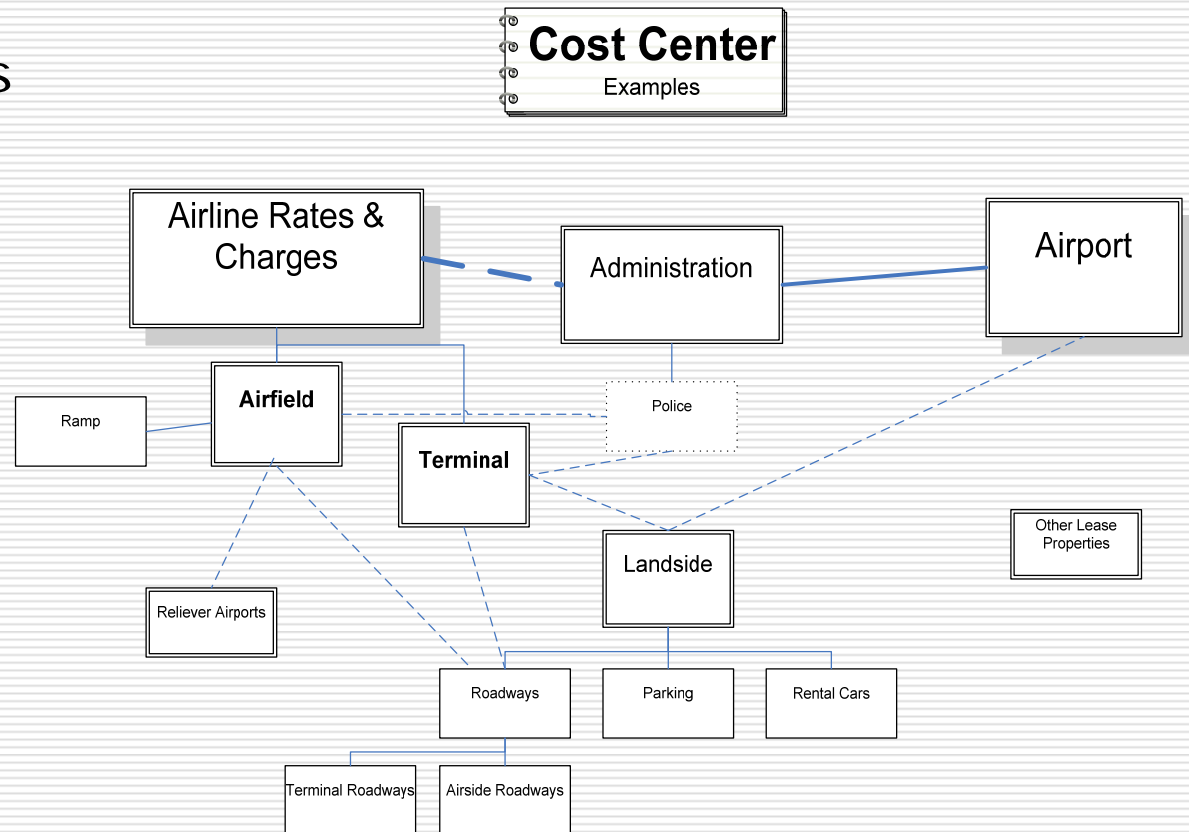
UNRESTRICTED CASH BALANCES AT LARGE HUB AIRPORTS



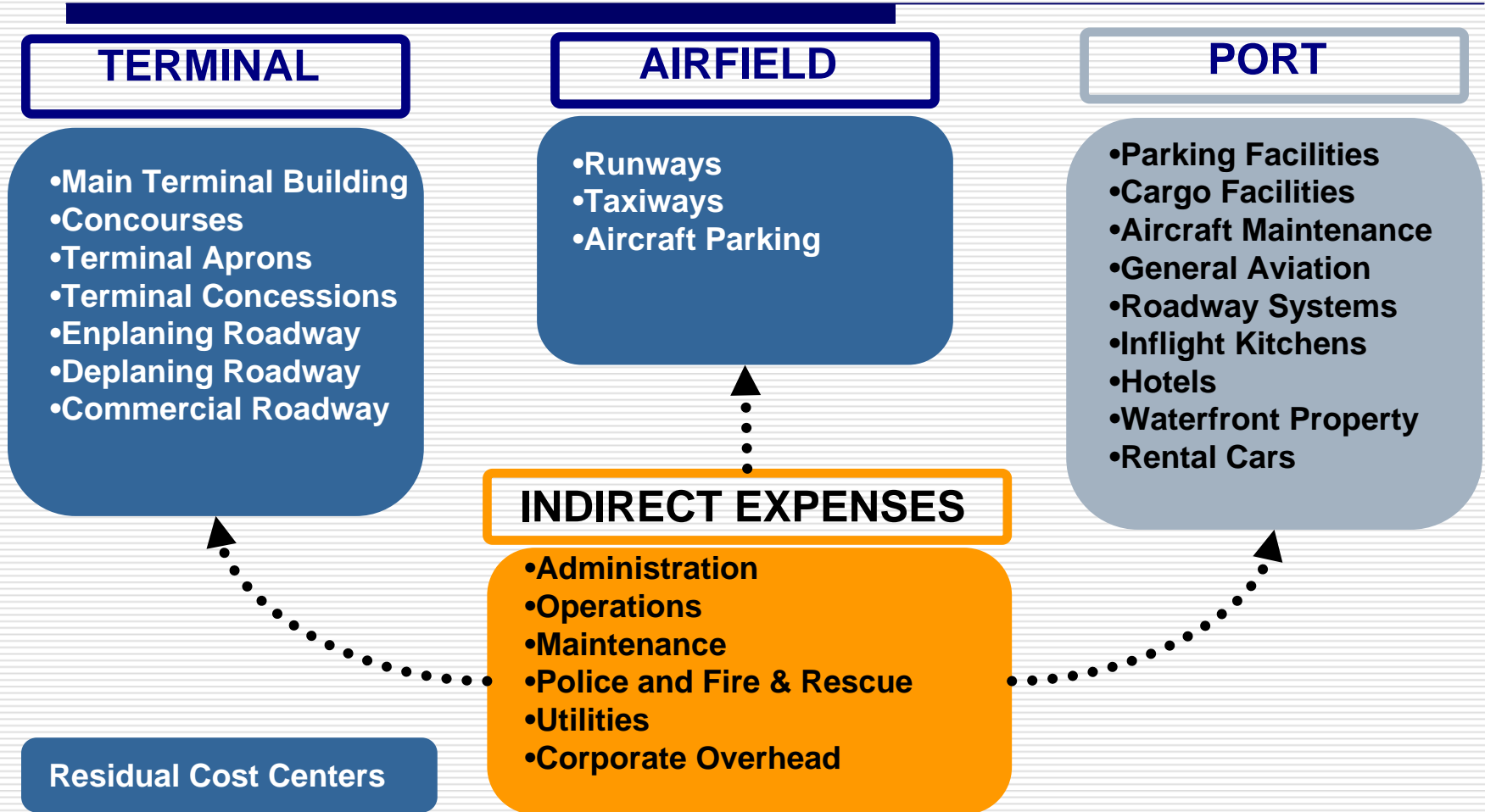
Interdependence: Allocation of Revenues and Costs, and Business Deal

- Allocation of revenues and costs has implications for:
 - Rates
 - Risks
 - Management

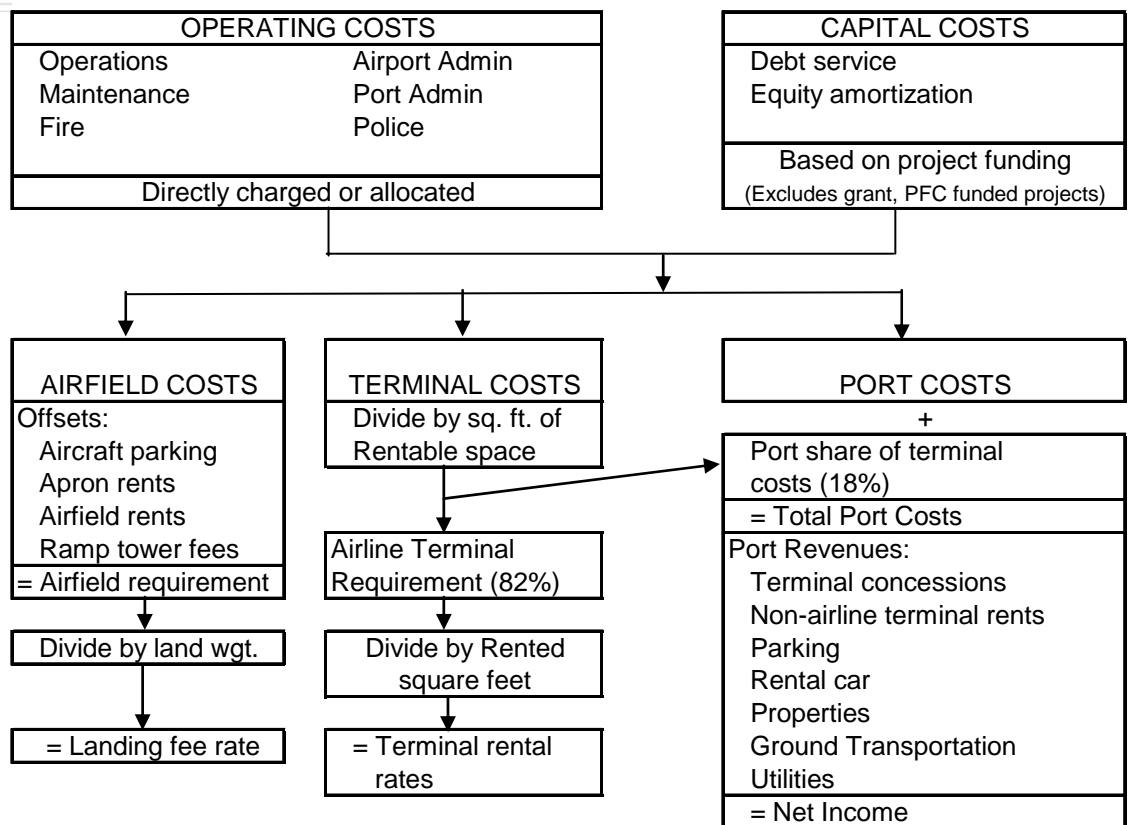
- **Key issue**--What portions get allocated to airline cost centers and how are they distributed to the airline rate-bases



Portland: Cost Center and Rates and Charges Methodologies



Seattle-Tacoma: Rates and Charges Fundamentals



Business Deal

- Airfield is a cost center residual
- Terminal is commercial compensatory residual (no vacancy risk)

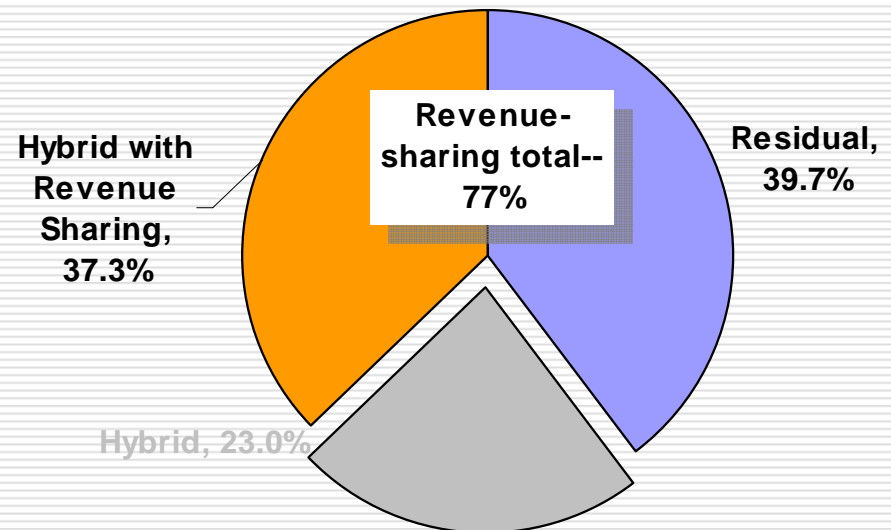
Allocations

- Roadway cost allocation: 25% terminal, 25% Airfield and 50% Port
- Debt service coverage: rate base coverage = zero unless needed to achieve 1.25x overall coverage

Revenue Sharing—Industry Trends

- About 77% of large hub airports have revenue sharing
 - Cost center specific or
 - Airport-wide
- Why?
- Emerging Trends/Concepts
 - Extraordinary coverage protection
 - Share revenues after all costs are reimbursed (including Airport equity)

RATE MAKING METHODOLOGIES
Top 29 Large Hub Airports



Ranked by passengers. Hybrid includes the use of compensatory and residual rate-making methodologies. Results do not include HNL.

“Bottom-Line” Protections & Incentives: Any Difference between Compensatory and Residual?

Residual Deals

- Guaranteed payment of operating expenses and debt service
- Increased discretionary funds through expense savings

Hybrid with/without Revenue Sharing

- Rate covenant protections
- Minimum coverage levels
- Extraordinary coverage protection

Rates & Charges Q&A
