EMERGING TRENDS IN USE AND LEASE AGREEMENTS

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INTRODUCTION

- Advanced session focused on specific issues
- Overview of current trends
- Plan for future
- The BIG issues
- Quick review
  - Negotiated agreement vs. rates by ordinance
  - Legal requirements and constraints
  - Know your airport
CURRENT TRENDS

- Contrasting business models
  - Legacy, low cost carrier, ULCC
  - Start-ups (Moxie? One Jet? Midwest Express 2?)
- Alignment of airlines – “them” vs. “the other guys”
- Airline consortia
- Current business situation
- Planning for the future
BACKGROUND - REFRESHER

- The legal issues
  - No *unjust* discrimination
  - Reasonable, transparent rates
  - Self sustaining requirement
  - Rates and charges policy
  - Airport indenture requirements

- Agreement vs. ordinance
  - Good faith negotiations
  - Compensatory vs. residual rates

- Know your airport
  - Sources and uses of funds
  - Cost centers and cost recovery
# Airports with Rates by Ordinance

<table>
<thead>
<tr>
<th>Airport</th>
<th>Hub Size</th>
<th>CY 2016 e.p. (Approved)</th>
<th>Time Under Resolution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Los Angeles International</td>
<td>L</td>
<td>39,635,691</td>
<td>Since 1993¹</td>
</tr>
<tr>
<td>Phoenix Sky Harbor International</td>
<td>L</td>
<td>20,896,229</td>
<td>&gt; 30 years</td>
</tr>
<tr>
<td>Orlando International</td>
<td>L</td>
<td>20,283,479</td>
<td>Effective November 2013²</td>
</tr>
<tr>
<td>Boston Logan International</td>
<td>L</td>
<td>17,749,202</td>
<td>&gt; 30 years</td>
</tr>
<tr>
<td>Oakland International</td>
<td>M</td>
<td>5,934,839</td>
<td>Since 2000</td>
</tr>
<tr>
<td>Raleigh-Durham International</td>
<td>M</td>
<td>5,378,837</td>
<td>&gt; 30 years</td>
</tr>
<tr>
<td>John Wayne Airport-Orange County</td>
<td>M</td>
<td>5,217,242</td>
<td>&gt; 20 years</td>
</tr>
<tr>
<td>Omaha Eppley Airfield</td>
<td>M</td>
<td>2,125,319</td>
<td>&gt; 30 years</td>
</tr>
<tr>
<td>Charleston International</td>
<td>S</td>
<td>1,884,036</td>
<td>Since 2001</td>
</tr>
<tr>
<td>Grand Rapids Gerald R. Ford International</td>
<td>S</td>
<td>1,334,833</td>
<td>&gt; 30 years</td>
</tr>
<tr>
<td>Long Beach/Daugherty Field</td>
<td>S</td>
<td>1,360,357</td>
<td>At least 10 years</td>
</tr>
<tr>
<td>Des Moines International Airport</td>
<td>S</td>
<td>1,214,307</td>
<td>Since January 1, 2014</td>
</tr>
<tr>
<td>James M Cox Dayton International</td>
<td>S</td>
<td>1,017,941</td>
<td>?</td>
</tr>
<tr>
<td>Greenville Spartanburg International</td>
<td>S</td>
<td>990,512</td>
<td>Since July 2016</td>
</tr>
<tr>
<td>Bill &amp; Hillary Clinton National (Little Rock)</td>
<td>S</td>
<td>958,824</td>
<td>Since 2009</td>
</tr>
<tr>
<td>Greensboro International</td>
<td>S</td>
<td>846,042</td>
<td>Since 1999</td>
</tr>
<tr>
<td>Fresno Yosemite International</td>
<td>S</td>
<td>761,298</td>
<td>Since July 2016</td>
</tr>
<tr>
<td>Akron-Canton Regional</td>
<td>S</td>
<td>685,269</td>
<td>Since January 1, 2015</td>
</tr>
<tr>
<td>Northwest Arkansas Regional</td>
<td>S</td>
<td>670,528</td>
<td>Since January 1, 2015</td>
</tr>
<tr>
<td>Lexington Blue Grass</td>
<td>S</td>
<td>638,316</td>
<td>Since 2001</td>
</tr>
<tr>
<td>Eugene Mahlon Sweet Field</td>
<td>N</td>
<td>483,078</td>
<td>?</td>
</tr>
<tr>
<td>Asheville Regional</td>
<td>N</td>
<td>416,911</td>
<td>Since October 2016</td>
</tr>
<tr>
<td>Lehigh Valley International (Allentown, PA)</td>
<td>N</td>
<td>324,151</td>
<td>Since 1993</td>
</tr>
<tr>
<td>Santa Barbara Municipal</td>
<td>N</td>
<td>329,751</td>
<td>Since October 2007</td>
</tr>
<tr>
<td>Rapid City Regional</td>
<td>N</td>
<td>272,389</td>
<td>Since 2016</td>
</tr>
<tr>
<td>Aspen/Pitkin County Airport</td>
<td>N</td>
<td>254,354</td>
<td>Since 2001</td>
</tr>
<tr>
<td>Lafayette Regional</td>
<td>N</td>
<td>205,239</td>
<td>?</td>
</tr>
</tbody>
</table>

**Transitioned from Ordinance to Airline Agreement**

<table>
<thead>
<tr>
<th>Airport</th>
<th>Hub Size</th>
<th>CY 2016 e.p. (Approved)</th>
<th>Time Under Resolution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sacramento International</td>
<td>M</td>
<td>4,969,337</td>
<td>June 2008 - July 2017, then new agreement</td>
</tr>
<tr>
<td>San Juan Luis Munoz Marin International</td>
<td>M</td>
<td>4,327,833</td>
<td>&gt; 20 years, but airport privatized March 2013</td>
</tr>
</tbody>
</table>


² The LAX landing fee tariff, as amended from time to time, has been in effect since July 1, 1993, and was the subject of two rate disputes (LAX I and II).

³ Airlines that sign the 3-year “Rate and Revenue Sharing Agreement” are eligible for revenue sharing and commit to not challenge the ratemaking methodology.

Source: Compiled by Leight/Fisher
## AIRPORT RATE METHODOLOGIES

<table>
<thead>
<tr>
<th>Methodology</th>
<th>Large Hubs</th>
<th></th>
<th>Medium Hubs</th>
<th></th>
<th>Total</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number</td>
<td>Percent</td>
<td>Number</td>
<td>Percent</td>
<td>Number</td>
<td>Percent</td>
</tr>
<tr>
<td>Residual</td>
<td>8</td>
<td>27%</td>
<td>11</td>
<td>35%</td>
<td>19</td>
<td>31%</td>
</tr>
<tr>
<td>Compensatory</td>
<td>9</td>
<td>30%</td>
<td>9</td>
<td>29%</td>
<td>18</td>
<td>30%</td>
</tr>
<tr>
<td>Hybrid</td>
<td>13</td>
<td>43%</td>
<td>11</td>
<td>35%</td>
<td>24</td>
<td>39%</td>
</tr>
<tr>
<td></td>
<td>30</td>
<td>100%</td>
<td>31</td>
<td>100%</td>
<td>61</td>
<td>100%</td>
</tr>
</tbody>
</table>

| Form of Agreement | Large Hubs |   | Medium Hubs |   | Total |   |
|                  | Number     | Percent | Number      | Percent | Number | Percent |
| Ordinance        | 4          | 13%     | 6           | 19%     | 10     | 16%     |
| Agreement        | 26         | 87%     | 25          | 81%     | 51     | 84%     |
|                  | 30         | 100%    | 31          | 100%    | 61     | 100%    |

Source: Compiled by LeighFisher
Cost Centers: Functional areas or activities of an airport or airport system used for the purposes of accounting for revenues, operating expenses, amortization, and debt service.
CURRENT TRENDS – CONTEXT FOR NEGOTIATIONS

Thinking like an airline (it’s not that hard)
NEW(ISH) BUSINESS MODELS

- ULCCs – domestic and international
  - Point-to-point
  - Unbundled
  - Nimble, opportunistic
  - Limited service
  - New choices for your customers
- Contrast with legacy carriers
  - Hub and spoke
  - Daily frequencies
  - Provide the bulk of service
- Smaller business-focused services
  - E.g., OneJet, Midwest Express 2, Silver
- New entrants
ALIGNMENT OF AIRLINES BY BUSINESS MODEL

- “Big 4” vs. the others
  - Policies designed to reduce competition
  - Are these models really incompatible?
- Challenge – airport rates that allow ALL airlines to thrive
- Requires strategic approach
CURRENT REALITY

- Less PFC capacity
- Reduced AIP funding
- Aging facilities = BIG projects
- Facility constraints, growth in service
- Revenue mix
  - Larger airports: concessions, esp. parking
  - Low aeronautical rates
  - Cost recovery
PLANNING FOR THE FUTURE

- Impact of TNCs
- Turo’s impact
- Potential impact of autonomous unmanned vehicles (AUVs)
- New entrants and new business models
- Other disruptive technologies, e.g.,
  - Uber Elevate
  - Facial recognition
  - Part 380 operations
BIG ISSUES

It’s all about how risk is allocated
PRIMARY AREAS OF CONTENTION

- Allocation of common use fees
- Term
- MII, CIP approval
- Per turn fees
- Recovery of airline space
- Use of CUTE
- Cost center allocation
- Rates by ordinance vs. agreement
This may be the hottest current issue
One size does NOT fit all!
80-20 model is no longer the norm
  • Retention of a fixed component impacts infrequent service & larger carriers
Use of activity as one or more metrics
  • Enplaned passengers
  • Bags handled
  • Operations/turns
  • Impacts on different carriers
Use allocation methodology to drive behaviors, recover costs
METHODS OF RECOVERING BHS COSTS

SUMMARY

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>80/20 (passengers/users)</td>
<td>24</td>
<td>38%</td>
</tr>
<tr>
<td>90/10 (passengers/users)</td>
<td>8</td>
<td>13%</td>
</tr>
<tr>
<td>90/10 (bags/users)</td>
<td>1</td>
<td>2%</td>
</tr>
<tr>
<td>100% pax</td>
<td>11</td>
<td>17%</td>
</tr>
<tr>
<td>100% bags</td>
<td>11</td>
<td>17%</td>
</tr>
<tr>
<td>Other/Exclusive sq ft</td>
<td>8</td>
<td>13%</td>
</tr>
<tr>
<td>Total</td>
<td>63</td>
<td>100%</td>
</tr>
</tbody>
</table>

Carveouts (BWI, CMH, IND, PHX, SDF); small airline bucket (STL), 100% bags O&M (CLT), ULCC terminals (AUS, MSP, TUS); EDS 100% bags (SNA), turn fee (SFO)

DCA, IAD, SAN have carveout

Source: Compiled by LeighFisher from various sources, October 2019.
AGREEMENT TERM

- Trending shorter, but
  - ULCCs prefer shorter
  - Big 4 prefer longer especially where large capital programs
- Term also affects justification for non-signatory penalty
- Options include:
  - Term with options (mutual or MII)
  - Planned holdover
  - Evergreen
  - May depend on bond market perception/requirements
COMMON USE SPACE & RECOVERY OF SPACE

- Accommodate new entrants, growth of incumbents
- Variable/less frequent use
- “Use it or lose it” recapture provisions
  - Gates
  - Other facilities: ticket counters, RON, office space
  - Appropriate metrics for measuring & allocating use
- Exclusive, preferential and common or joint use space (and when they are indistinguishable), and public areas
  - Impact of funding source (e.g., PFCs cannot be used to fund long term exclusive use leased space)
## FACILITY CONTROL

<table>
<thead>
<tr>
<th>Lease Type</th>
<th>Description</th>
<th>Example Types of Space</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exclusive</td>
<td>Exclusive right to use</td>
<td>Ticket counter, back office, clubrooms</td>
</tr>
<tr>
<td>Preferential</td>
<td>First right, airport may assign others if not in use</td>
<td>Gates, holdrooms, ticket counters</td>
</tr>
<tr>
<td>Joint</td>
<td>Multiple airlines use jointly</td>
<td>Baggage handling - Avoid paying costs of others</td>
</tr>
<tr>
<td>Common</td>
<td>Airport assigns</td>
<td>Gates, ticketing, FIS, Circulation, restrooms</td>
</tr>
</tbody>
</table>
DEFINING TERMINAL SPACE

- Define rentable vs. non-rentable space
  - Cost recovery for non-rentable space
  - Commercial compensatory vs. other methods
- Common use space
  - Airline
  - Public
- Joint use space
- Any exclusive use space?
- Virtual preferential space
NEW MCO GATE ASSIGNMENTS – NO MORE PREFERENTIAL GATES

- **Annual Access Gate**
  - Annual Access Gate: Airline pays annual fee for access to Gate assigned the Authority.
  - Airline must declare the number and type of Annual Access Gates required each period.
  - Location of Gate(s) may change as needed.
  - Gates may be granted priority access.

- **Priority Access Gates**
  - Airline may request Priority Access if activity meets Utilization Threshold
  - Utilization Threshold for the initial year is 6.0 turns per Gate per day; recalculated once per year
  - Priority Access Gates subject to availability as determined by the Authority.
  - Authority will work with Airline to schedule flight activity on the Priority Access Gates

- **Common use per turn**
KEY LEVERS TO RECOVER AIRPORT COSTS

- Debt service coverage
- Amortization & imputed interest
- PFC off-sets
- Direct & indirect cost centers
  - Recover ALL costs
- O&M allocations
  - ARFF
  - Security
  - Administration
  - Common areas
PER TURN FEES

- For low frequency and legacy carriers
- Retain control over % of gates?
- Dynamic pricing – incentivize appropriate behaviors
  - Leased gate vs. use per turn?
  - Recover costs
  - Who receives payment for use of preferential gate?
- Several variables in turn fee
  - Average numbers of turn per day (over a year) per gate
  - Fully loaded cost – holdroom, loading bridge, ramp, ticket counter, FIS, other?
  - Non-signatory (or other) premium?
  - Premium for multiple uses per day?
CUTE

- Less use of common use terminal equipment in U.S.
- Desire by airlines for proprietary equipment
  - Proprietary back walls & systems
  - CUTE often not 100% compatible
  - Data protection
- Technological change – good & bad
  - More flexible use of facilities
  - Trend towards e-tickets
  - Allocation of O&M responsibility, liability and cost
MAJORITY-IN-INTEREST (OR MOTHER MAY I?)

- Whose airport is this anyway? Who bears the risk?
- Airport: address local needs, provide for competition
- Airlines: risk of cost of new facilities, desire to prevent competition
- Appropriate metric(s) can include number of signatories, enplaned passengers, landed weights, payments to airport
- Wide range of alternatives, from none to strong MII
  - Pre-approved CIP; other projects (in excess of $X) subject to MII
  - Negative MII; high or low bar
  - Deferral vs. rejection
  - Rates by ordinance, with no MII
  - Annual basket of discretionary capital revenues
AIRLINE INVOLVEMENT IN CIP

- Role of Airline Technical Rep
  - Increased airline input
    - MCI
    - PIT
- Airline-driven/funded projects
  - SWA at HOU, DAL
  - Delta BOS Terminal A
<table>
<thead>
<tr>
<th></th>
<th>Program Management Committee</th>
<th>Steering Committee (SC)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Purpose</strong></td>
<td>Supports the SC by providing overall management and coordination</td>
<td>Review/approve any changes to all Threshold Issues</td>
</tr>
<tr>
<td><strong>Members</strong></td>
<td>1. KCAD - Deputy Director</td>
<td>1. KCAD - Director of Aviation</td>
</tr>
<tr>
<td></td>
<td>3. Developer – VP/Managing Director for TMP</td>
<td></td>
</tr>
<tr>
<td><strong>Responsibilities</strong></td>
<td>1. Prepare and submit appropriate documents to the SC</td>
<td>1. Set Program Policy and provide Program oversight</td>
</tr>
<tr>
<td></td>
<td>2. Establish/review baselines, scope, cost estimates, schedules</td>
<td>2. Review and resolve issues to maintain forward progress in achieving Program goals</td>
</tr>
<tr>
<td></td>
<td>3. Establish clear lines of responsibility, authority, and communication (spirit of teamwork</td>
<td>3. The SC is responsible for the following:</td>
</tr>
<tr>
<td></td>
<td>among all stakeholders)</td>
<td>a. Overall Program review and approval</td>
</tr>
<tr>
<td></td>
<td>4. Minimize Program impacts on Airport operations, operating airlines, and other tenants</td>
<td>b. Decision making authority within the Program for all procurements</td>
</tr>
<tr>
<td></td>
<td>5. Coordinate projects with other on-going Airport projects</td>
<td>c. Review and approval of all TMP’s scope, cost and schedule</td>
</tr>
<tr>
<td></td>
<td>6. Ensure proper review and approval by the SC before contracts for services or construction</td>
<td>d. Review Bid Packages before released for bidding</td>
</tr>
<tr>
<td></td>
<td>are developed and executed</td>
<td>e. Review and advise bid awards</td>
</tr>
<tr>
<td></td>
<td>7. Review performance of consultant and construction contractors providing</td>
<td>f. Review weekly, monthly and quarterly reports</td>
</tr>
<tr>
<td></td>
<td>services to the Program and review quality standards</td>
<td>g. Review financial controls recommendations and reports</td>
</tr>
<tr>
<td></td>
<td>8. Coordinate both internal and external interfaces, identify any issues, and obtain</td>
<td></td>
</tr>
<tr>
<td></td>
<td>resolution</td>
<td></td>
</tr>
<tr>
<td></td>
<td>9. Direct the value engineering exercises to satisfy the required function at the lowest</td>
<td>4. The SC shall review any part of the Program that has deviated from its SC approved</td>
</tr>
<tr>
<td></td>
<td>cost consistent with performance, reliability and maintainability requirements</td>
<td>baseline scope, budget or schedule. Developer shall recommend subsequent corrective</td>
</tr>
<tr>
<td></td>
<td>10. Review all significant deviations from the Program baseline as established</td>
<td>actions based on the following criteria:</td>
</tr>
<tr>
<td></td>
<td>11. Review all packages of work</td>
<td>a. Scope Changes</td>
</tr>
<tr>
<td></td>
<td>12. Approve all change orders that do not materially affect Airline operations, Program</td>
<td>b. Schedule delays over the baseline</td>
</tr>
<tr>
<td></td>
<td>Schedule, or Program scope, or that affect the payments required of the Airlines under the</td>
<td>c. Budget variances over or under the baseline</td>
</tr>
<tr>
<td></td>
<td>Airline Use and Lease Agreement (“Threshold Issues”)</td>
<td></td>
</tr>
</tbody>
</table>
AIRLINE CONSORTIA

- End run around airport rate setting?
- What services appropriate?
- Can airlines opt out?
- Governance model; airport input
- Role of ground handlers
FINAL THOUGHTS

- Question authority – "we’ve always done it this way” – Really?
- Understand your market and your airlines
- Your airport is different – structure for your unique situation
- These issues are all interrelated – the best solution may require several parts
- Plan for the future
QUESTIONS AND OBSERVATIONS

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