

21ST ANNUAL AIRPORT LAW WORKSHOP

AIRPORT FINANCIAL ISSUES

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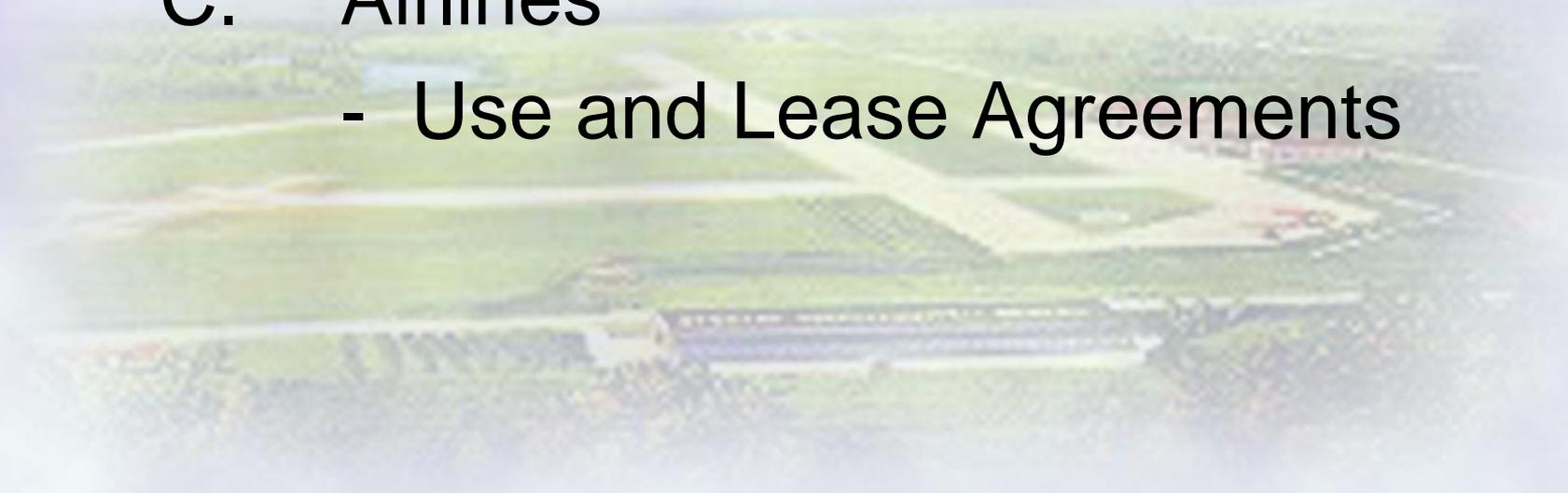
STEVE KAPLAN

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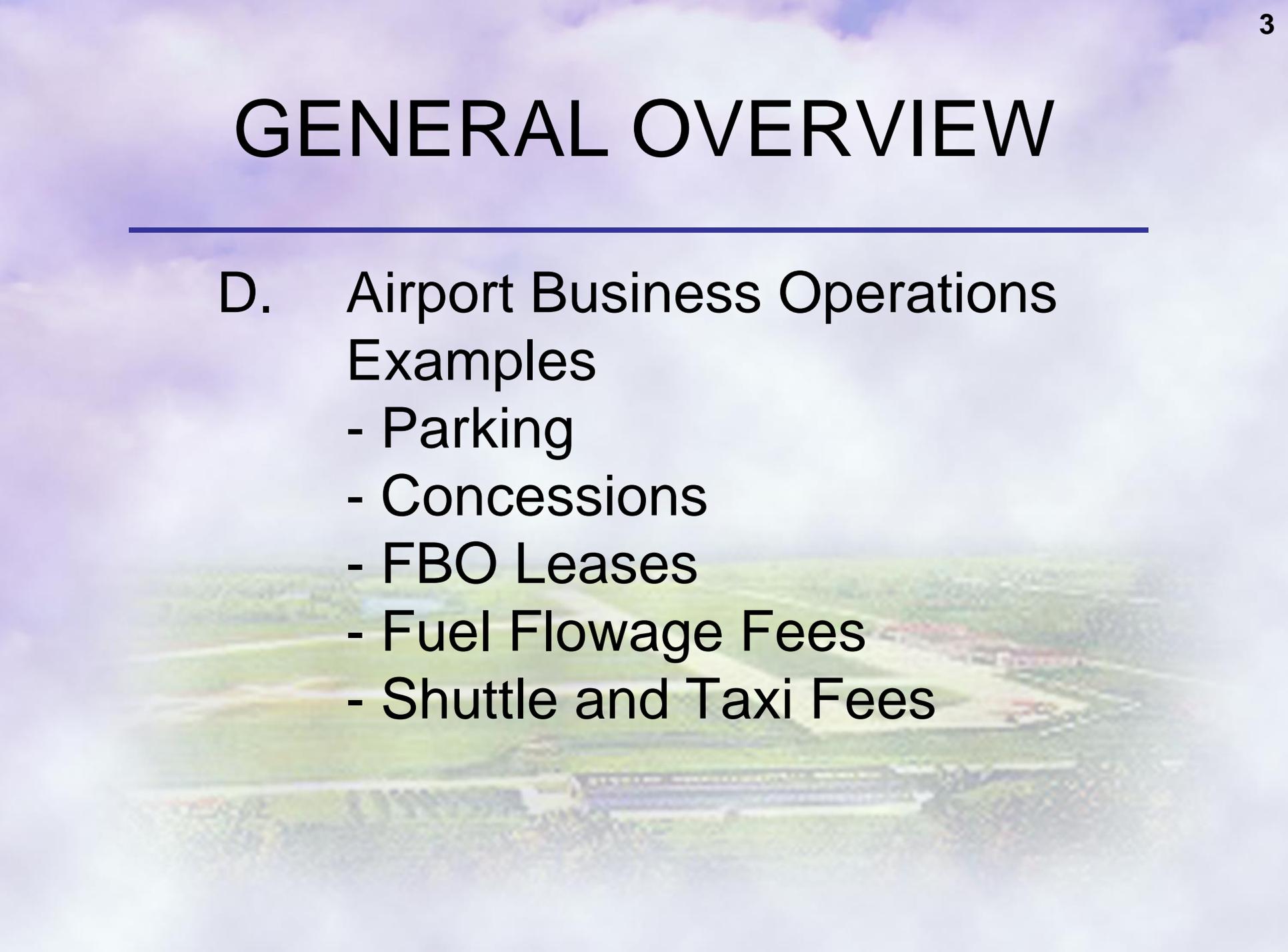


GENERAL OVERVIEW

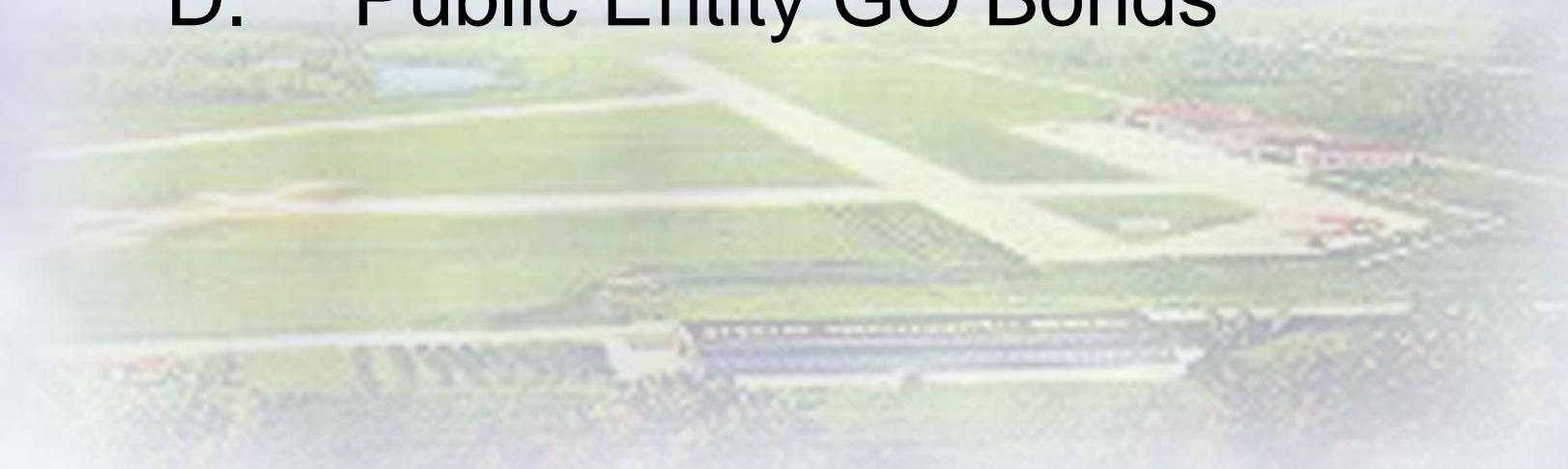
- WHERE DO AIRPORTS GET FUNDING?
 - A. AIP Grants (Federal)
 - B. PFCs (Federally Approved)
 - C. Airlines
 - Use and Lease Agreements



GENERAL OVERVIEW

- D. Airport Business Operations
- Examples
- Parking
 - Concessions
 - FBO Leases
 - Fuel Flowage Fees
 - Shuttle and Taxi Fees
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- An aerial photograph of an airport terminal and surrounding runways, serving as a background for the slide. The terminal is a large, modern building with a glass facade, and the runways are visible in the foreground and background.

HOW CAPITAL PROJECTS ARE FINANCED

- A. Airport Revenue Bonds
 - B. Special Facilities Bonds
 - C. PFC Bonds
 - D. Public Entity GO Bonds
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- An aerial photograph of an airport terminal and runways, showing a large terminal building with a blue roof and several runways extending into the distance. The image is slightly faded and serves as a background for the lower portion of the slide.

KEY AIRPORT FINANCIAL PRINCIPLES

- Airport – As self-sustaining as possible
- Funds are to be used for aviation-related activity
- Funds may not be used for off-airport activities (Revenue Diversion)
- Funds may not be shared with a public entity unless for a specific airport purpose (Revenue Diversion)

KEY AIRPORT FINANCIAL PRINCIPLES

- AIP funds require grant assurances with FAA
- PFCs require similar agreements
- Airports have slightly more latitude with PFCs
- Airports have somewhat more latitude with airport-generated revenues such as parking, concessions

TOPICS IN THIS SESSION

- Airport Improvement Program Funding
 - Passenger Facilities Charges
 - Revenue Diversion
 - Rates and Charges
 - Hypothetical Problems
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- An aerial photograph of an airport terminal and runways, showing the layout of the airport and surrounding greenery. The terminal is a large, modern building with a glass facade, and the runways are visible as long, straight paths. The background shows a mix of green fields and some buildings.

AIRPORT IMPROVEMENT PROGRAM

- Federal - Airport and Airway Trust Fund
 - Entitlement
 - Discretionary
 - Grant Assurances
 - Permitted Uses
 - Prohibited Uses
 - LOIs
- 
- An aerial photograph of an airport terminal and runways, showing the terminal building, taxiways, and runways stretching into the distance. The image is slightly faded and serves as a background for the lower portion of the slide.

AIP

ENTITLEMENT FUNDS

- Primary Airports – formula based on number of boarding passengers
 - Small Airport Fund
 - Cargo Service Airports
 - States/Insular Areas
 - Nonprimary Airports
 - Alaska Supplemental Funds
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- An aerial photograph of an airport terminal and runways, showing the layout of the airfield and surrounding landscape.

AIP

DISCRETIONARY FUNDS

- Set-Asides
- Remaining Funds
- National Priority System
- Work should be commenced soon
- Noise – 35% of Discretionary Funds –
Noise Compatibility/Mitigation
- Military Airport Program – 4%
- Reliever – 0.66%

AIP

PROJECT REQUIREMENTS

- NEPA Compliance
- Work items must be located with the airport boundary, with limited exceptions, such as noise implementation projects, utility construction, relation of roads, environmental mitigation
- Airport matching funds

AIP

PROJECT ELIGIBILITY

- Airport Planning
- Airport Development
- Airport Noise Compatibility Planning
- Airport Noise Compatibility Implementation



AIRPORT DEVELOPMENT PROJECTS

- **Constructing, repairing, or improving a public use airport**
- **Acquiring for or installing items such as NavAids, safety or security equipment**
- **Acquiring an interest in land or airspace for an airport development project or address airspace hazards**
- **Constructing or relocating a control tower**
- **Complying with ADA and certain environmental laws**

AIRPORT DEVELOPMENT PROJECTS

- Deicing pad, activities
 - Preserve life of runways at non-hub and non-primary airports
 - Acquiring baggage and ground transportation equipment
 - Clean air-related acquisitions
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- An aerial photograph of an airport terminal and runways, serving as a background for the slide. The terminal is a large, modern building with a glass facade, and the runways are visible in the distance. The image is slightly faded and has a soft focus.

AIP

PROJECT ELIGIBILITY

- Prohibitions
 - Decorative landscaping, art work (architectural features permitted)
 - Public parking for passenger cars
 - Hangars except at non-primary airports
 - Any part of an airport building except eligible facilities

PASSENGER FACILITIES CHARGES

- FAA must approve application; notice to carriers and public comment
- \$1, \$2, \$3 per paying passenger boarding an aircraft at the airport
- \$4, \$4.50 at larger airports (Specific Criteria) with AIP offset
- Used for airport-related project
- Not federal funds or airport revenue

PASSENGER FACILITIES CHARGES

- Assurances similar to AIP Grant Assurances
- Greater flexibility than with AIP Funds
- May be used to back bonds



PFC

PROJECT ELIGIBILITY

- Must be an eligible airport-related project
 - Revenue generated cannot exceed amount of PFCs; and
 - Preserve or enhance capacity, safety or security of the national air transportation system; or
 - Reduce noise; or
 - Enhance competition among carriers

PFC

PROJECT ELIGIBILITY

- If in excess of \$3 for an eligible surface transportation or terminal project, airside needs must have been met



PFCs = AIP OFFSET

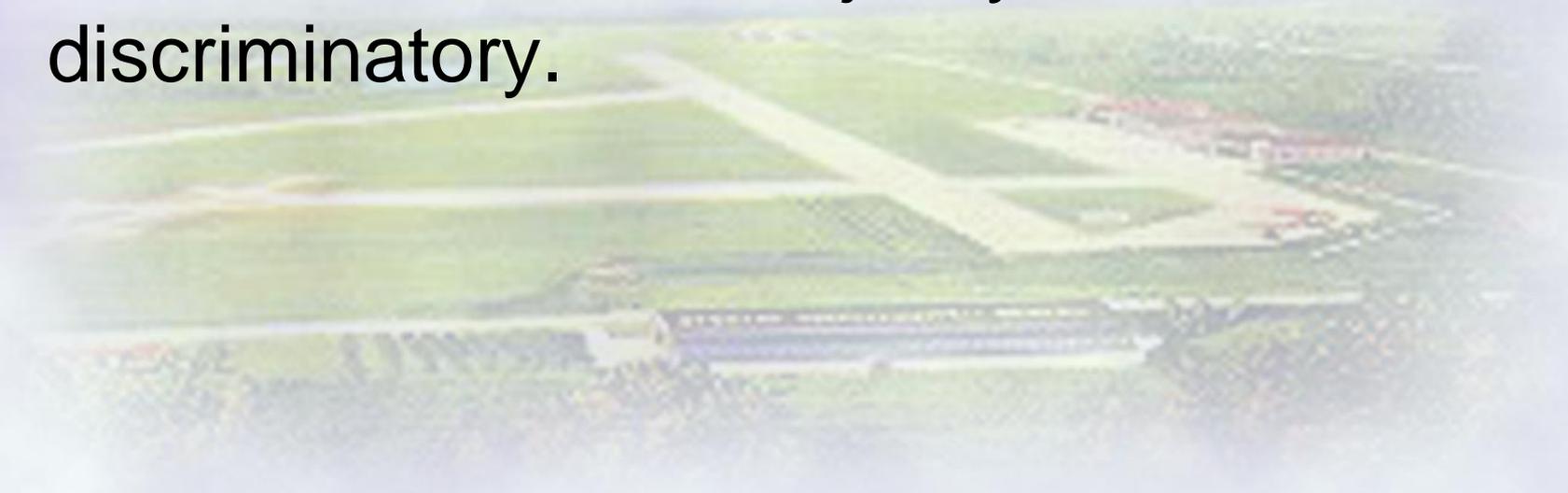
- Large, medium hubs with a PFC of \$3 or less have AIP entitlement reduced by 50%
- If the PFC is higher than \$3, the reduction is 75%
- Overall, some large airports are considering not taking any AIP funds to gain more flexibility, fewer restrictions

FAA Policy Regarding Airport Rates and Charges



WHAT DOES THE RATES AND CHARGES POLICY DO?

- Provides comprehensive guidance on the legal requirements that airport fees be reasonable and not unjustly discriminatory.



WHERE DO THESE REQUIREMENTS COME FROM?

Anti-Head Tax Act (49 U.S.C. 40116(e)(2))

- permits States and local governments to levy or collect reasonable rental charges, landing fees, and other service charges from aircraft operators using airport facilities.

49 U.S.C. 47129, "Resolution of airport-air carrier disputes concerning airport fees" (Expedited Procedures) (rules at 14 C.F.R. Part 302, Subpart F)

- Incorporates reasonableness requirement.
- DOT determines whether fee at issue is reasonable or unreasonable but does not set the fee.

49 U.S.C. 47107(a)(1)(2)(13), the former
Airport and Airway Improvement Act of
1982, as amended

- requires that recipients of FAA airport development grants make the airport available for public use on reasonable conditions and without unjust discrimination.
- air carriers using airport must be subject to substantially comparable charges.
- under self-sustaining requirement, airport's charges for use of facilities and services must make the airport as self-sustaining as possible under the circumstances existing at the airport.

THE RATES AND CHARGES POLICY IS INTENDED TO:

- Provide guidance to airport proprietors and aeronautical users.
- Encourage direct negotiation between parties.
- Minimize need for direct Federal intervention.
- Establish standards that FAA will apply in addressing airport fee disputes and compliance issues.

I. FAA reliance on airports and users to assure reasonable fees without Federal intervention.

- The issue of rates and charges is best addressed at the local level by agreement between users and airports.
- Airport proprietors and users should consult on fees.
- FAA would prefer relying upon airport proprietors, aeronautical users, and the market to ensure compliance with legal requirements.

II. Airport fees must be reasonable

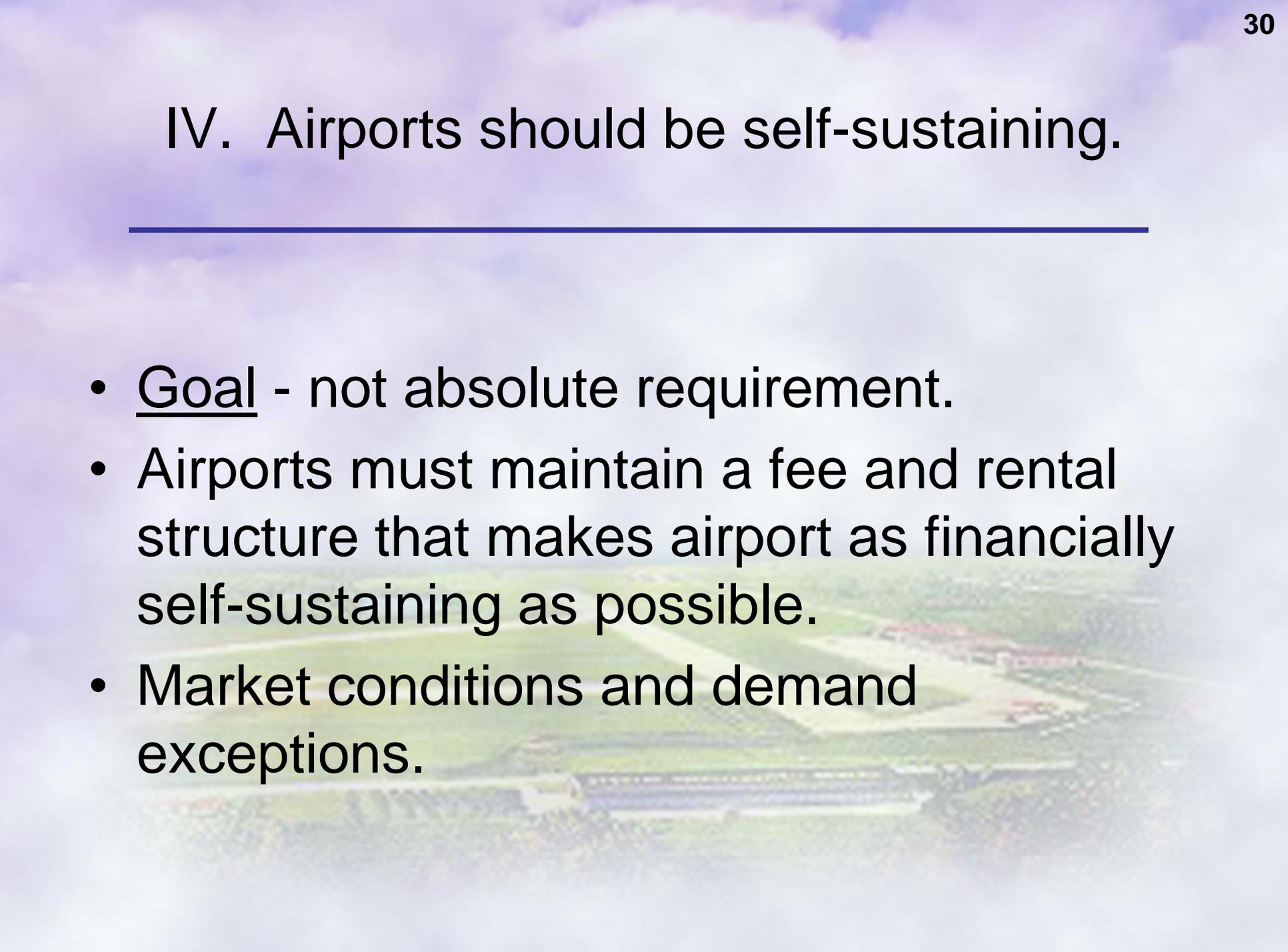
- Federal law has long imposed a reasonableness requirement on fees charged by airports to aeronautical users.



III. Unjust discrimination is prohibited.

- Aeronautical fees may not be unjustly discriminatory.
- Consistent methodologies - important.
- Reasonable distinctions OK among aeronautical users.
- Properly structured peak-period pricing systems could be OK.

IV. Airports should be self-sustaining.

- Goal - not absolute requirement.
 - Airports must maintain a fee and rental structure that makes airport as financially self-sustaining as possible.
 - Market conditions and demand exceptions.
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- An aerial photograph of an airport terminal and runways, serving as a background for the slide. The terminal is a long, blue-roofed building with a glass facade. Runways and taxiways are visible, along with some greenery and parking areas. The sky is overcast.

V. Airport revenues shall be used for airport purposes (49 U.S.C. §§ 47107(b) and 47133).

- Airport revenue must be applied for use of airport or sponsor facilities related to actual air transportation unless airport is grandfathered under statute.



Policy Application 1

- Policy applies only to *aeronautical* users of airport.
- However, FAA's self-sustaining requirement does extend to non-aeronautical fees.
- Therefore, non-aeronautical fees must be assessed at least at fair market value (i.e., they may exceed the costs of service) and may actually exceed FMV.

Policy Application 2

- Policy applies to fees set by contract, but a party to the contract can't file a complaint .
- Exception: Carriers may sign under protest if required to sign contract to obtain access to airport or signatory status, but have objected to that condition before signing.

Policy Application 3

- The Policy does not apply to general aviation airports or fees charged to general aviation users.



HOW AND WHERE ARE COMPLAINTS FILED CONCERNING RATES AND CHARGES?

- At an FAA Airport District Office or Regional Office on an informal basis.
- At FAA Headquarters through the 14 C.F.R. Part 16 formal complaint process.
- At DOT if the fee in question is imposed on an air carrier and a complaint is filed under the expedited airport-air carrier procedures, 49 U.S.C. 47129, 14 C.F.R. Part 302, Subpart F.

CURRENT STATUS OF FAA's RATES AND CHARGES POLICY

- Final policy issued June 21, 1996 (61 Fed. Reg. 31994).
- Air Transport Association (ATA) and the City of Los Angeles challenged policy in court. On August 1, 1997, the D.C. Circuit Court of Appeals “vacated” (*i.e.*, voided) five subsections of the policy which had established specific standards for reasonableness. Thus, these subsections are no longer technically operative.
- DOT/FAA had failed to justify the difference in treatment between airfield and non-airfield methodologies for calculating fees.

Rates and Charges Policy Status Continued ...

- In 1998, FAA issued advance notice of proposed rulemaking (ANPRM) seeking suggestions for replacement provisions for vacated portions of Policy. In 2003, FAA withdrew ANPRM because DOT/FAA are considering similar rate and charge issues in their review and study of congestion pricing at airports.
- With the enactment of AIR-21 (2000) and Vision-100 (2003), DOT/FAA focus on developing long-term policy options for managing capacity at LaGuardia and O'Hare, reviewing hub-dominated airports' competition plans, and studying congestion management options for busy airports generally.

Congestion Management Options Being Studied

- Proposed rule (2005) to manage congestion and delay at O'Hare through 2008.
- DOT/FAA considering various administrative and market-based mechanisms that may improve allocation of available capacity at airport where capacity is not able to meet aviation demand.

WHERE ARE WE NOW ?

- DOT/FAA will continue to determine reasonableness of fees – case-by-case – based on specific facts involved, portions of the policy not vacated, and precedent from various judicial and administrative decisions such as:
- Air Transport Association of America v. DOT (challenge to R&C Policy)
- Air Canada et al. v. DOT (Miami terminal case)
- City of Los Angeles v. DOT (LAX airfield opp. cost)
- Northwest Airlines, Inc. v. County of Kent
- New England Legal Foundation v. Massachusetts Port Authority

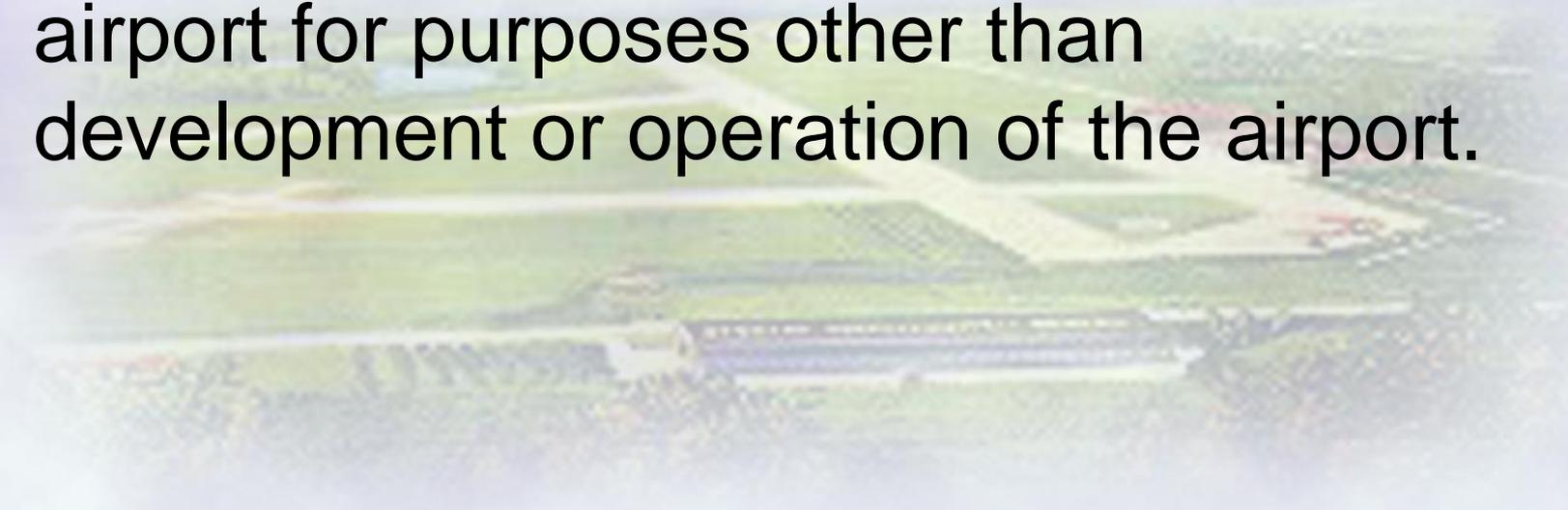
FAA's Revenue Use Policy: A Quick Review



“Revenue diversion”

What is it?

- Spending of revenue generated on an airport for purposes other than development or operation of the airport.



What's The Problem With Revenue Diversion?

- Undermines effectiveness of FAA's grant program.
- Burdens airport users with hidden taxation for unrelated municipal services and activities.

The General Requirement 49 U.S.C. § 47107(b))

- **All local taxes on aviation fuel (except taxes in effect on December 30, 1987) *and* the revenues generated by a public airport will be expended for the capital or operating costs of -**
- **the airport,**
- **the local airport system, or**
- **other local facilities owned or operated by the airport owner or operator and directly and substantially related to the air transportation of passengers or property.**

Revenue Diversion

“Grandfathering” Exemption:

- Requirement does not apply if airport is subject to (1) a law controlling financing, or (2) bond covenants or assurances, enacted not later than September 2, 1982, that require airport revenues to be used to support not only airport but also the general debt obligations or other facilities of the owner or operator.

Expansion of General Requirement in 1996 Statute (49 U.S.C. § 47133)

- Requirement applies to all airports receiving Federal assistance.
- Requirement applies to recipients of Federal financial assistance, not just grants.
- No expiration date.
- Two statutes of limitation.

Definition of Airport Revenue:

- Defined broadly ... all revenue received by the airport proprietor for operation of the airport, including revenue from sponsor activities on airport.

Permitted Uses of Airport Revenue – Some Examples:

- **Capital or operating costs of airport, local airport system, and other local facilities.**
- **Reimbursements to local govts. for costs of services actually received.**
- **Promoting competition – ads for new service.**
- **Cooperative advertising in some cases.**
- **Unreimbursed contributions if request made within 6 years.**
- **Lobbying and attorney fees to support activity consistent with the policy.**

Prohibited Uses of Airport Revenue 1

- Payments that exceed fair and reasonable value of services and facilities.
- Use of airport revenues for general economic development, marketing, and promotional activities unrelated to airport.

Prohibited Uses of Airport Revenue 2

- Loans of airport funds to state or local agency at less than prevailing interest rate.
- Impact fees assessed by any governmental body that exceed similar fees assessed against commercial or other governmental entities.

Prohibited Uses of Airport Revenue 3

- Land rental to or use of land by sponsor for nonaeronautical purposes at less than amount that would be charged commercial tenant (FMV or higher rate).
- Exception: for public recreational and other community uses in limited circumstances.

Prohibited Uses of Airport Revenue 4

- Use of land by sponsor for aeronautical purposes rent-free or for nominal rental rates.
- Exception: Not-for-profit aviation organizations, or police or fire-fighting units operating aircraft.

Prohibited Uses of Airport Revenue

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- Use of airport funds to support community activities or for support of community-purpose uses of airport property.
 - o Exception: Expenditures OK if directly related to operation or marketing of airport. If contribution minimal, FAA won't question if reasonable connection between recipient organization and local community acceptance of airport.
- Direct subsidy of air carrier operations.

Self-Sustaining Requirement 1 (Stealth Grant Assurance)

- Self-sustaining grant assurance included within revenue use policy.
- Your Old Friend, the General Rule: sponsor must maintain fee and rental structure that, in circumstances of its particular airport, will make airport as financially self-sustaining as possible.

Self-Sustaining Requirement 2

- Long-term goals/targets acceptable if market conditions or demand for air service hinder compliance.
- OK in some cases to operate at loss to retain aeronautical services.

Self-Sustaining Requirement 3

- Due to reasonableness requirement, self-sustaining requirement does not require airport to charge FMV rates to aeronautical users.
- Assurance satisfied by cost-based fees charged to aeronautical users.

Self-Sustaining Requirement 4

- **Airports should receive FMV for provision of nonaeronautical facilities and services to extent practicable.**
- **Exceptions:**
 - **Providing property for public community purposes.**
 - **Not-for-profit aviation organizations.**
 - **Military use of airport.**
 - **Use of airport for public transit systems.**

Financial Reporting Requirements

- Provide FAA and public annual report listing in detail, e.g., all amounts paid to other govt. units and purposes of payments.
- FAA may request from airports annual or special financial/operations reports.

Monitoring and Compliance:

- DOT-IG routinely audits airports for unlawful revenue diversion.
- FAA Airports Office conducts 2 audits per year.
- Annual reports, single audit reports, third-party complaints.
- Corrective action permitted.

Sanctions for Non-Compliance

- **Withhold future grants.**
- **Withhold payments under existing grants.**
- **Withhold approval of passenger facility charge (PFC) applications.**
- **Withhold non-aviation Federal transit funds.**
- **Assess civil penalties up to \$50,000.**
- **File suit in Federal district court to seek enforcement of an FAA order.**

What's New ?

- Air service development programs.
 - FAA Notice of Investigation to investigate whether Chicago illegally diverted \$1.5 million in airport revenue and used it to demolish Meigs Field runway and convert it to a city park.
 - Tax revenue from special airport tax districts.
 - FAA now conducting 2 audits per year.
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Hypotheticals



Hypothetical No. 1

T-Hangar Lease

Tiger Island Airport, a grant-obligated GA airport, offered an aircraft owner a 3-year permit for use of land upon which the aircraft owner would construct – at his expense – a T-Hangar. The pilot complained that 3 years was too short a time period – that he needed the permit for 10 years for planned business activities and that 3 years represented an insufficient time frame within which to amortize his investment. The pilot made a call to the local FAA Airports District Office to complain. What result? What result if the hangar was an existing hangar owned by the airport?

Hypothetical No. 2

Santa Pueblo Airport

Santa Pueblo Airport established a pavement maintenance program (PVP) which included a fee-based formula to defray the airfield's ongoing maintenance costs (due to environmental factors, wear and tear, etc.). The formula imposed a landing fee on aircraft weighing 10,000 lbs. or more. Aircraft weighing less than 10,000 lbs. were exempt. Fees range from \$2.90 for a 10,000 lb. aircraft to \$342.79 for a 60,000 lb. aircraft. For example, the operator of a Beechcraft Baron Twin would not be assessed any landing fee, the operator of a Cessna Citation 500 business jet would be assessed a landing fee of \$2.90, while the operator of a Gulfstream G-IV would be assessed a landing fee of \$324.67. The airport looks forward to developing a hefty revenue surplus with this fee structure to assist the airport maintain its pavement surface infrastructure. 92.5% of all operations at Santa Pueblo are by aircraft weighing less than 10,000 lbs. Is the PVP consistent with the FAA's rates and charges policy and Federal law? How about the revenue surplus?

Hypothetical No. 3

Athletic Fields at Johnny Carson International Airport

The State of California has decided that it would be good idea to promote the establishment of new athletic fields throughout the state in order to promote exercise and outdoor activity. A well-connected state staffer knows that there are ideal vacant fields at federally-funded Johnny Carson International Airport, operated by the City of Hope, California. The state approaches airport management – and the city government - with the ‘opportunity’ to take part in the new venture. The state offers to pay for all athletic field infrastructure (goal posts, grass, bleachers, etc.) but advises it lacks the funds to pay any land rental. In exchange for the infrastructure, the state demands a minimum lease period of 15 years. May the airport lease presently vacant airport land to the state with a 15 year lease?

Hypothetical No. 4

Hurricane Harriet

Airport A (medium/large hub, scheduled service) suffers damage from devastating Hurricane Harriet. The airport is shut down for a number of days. Other airports come to the rescue by providing various forms of assistance (humanitarian aid, technical support) to storm-ravaged Airport A and to accommodate evacuees traveling from City of Airport A to the relevant airport. Most of the airport sponsors used airport revenue to fund this ‘off-airport’ assistance to Airport A. That aid did not directly benefit the airport providing the assistance. Lawful or unlawful use of airport revenue?

Hypothetical No. 5

Maples, Florida

The City of Maples' Air Carrier Incentive Program pays an air carrier a revenue guarantee (city funds) to serve Maples International Airport. Is this unlawful revenue diversion?



Hypothetical No. 6

Promotional Incentives at John Adams Int'l Airport

The FAA's revenue diversion policy permits airports to provide promotional incentives for new service, limited to increasing the use of the airport and promoting competition. Adams Airport creates an incentive program that offers discounts (a break on landing fees) to air carriers for providing an increased number of seats but not flight frequencies. Is the incentive program consistent with the FAA's revenue use policy?

Hypothetical No. 7

Promotional Incentives at Oprah International Airport

Oprah International Airport management has received a number of unpleasant phone calls from local businesses (including some with their national headquarters located in Ophra), who complain of high airfares of the legacy carriers serving Ophra International. Airport management decide they need to attract a low-cost carrier (LCC) to help bring fares down so local businesses won't relocate. Airport staff contact a number of LCCs and a week later present the following options to airport management:

Accept an offer from LCC JetGreen Airways to enter into a joint marketing program to operate three daily round-trips with jet service to LaGuardia (LGA). JetGreen promises to use its best efforts to maximize seat sales on this and any future jet service using its normal marketing, advertising, and distributions programs. As an inducement for JetGreen to provide the jet service, the City of Ophra will guarantee JetGreen gross passenger revenues of \$5,000 per block hour for the OPR-LGA service for each daily scheduled round-trip jet service flight provided. The city agrees that JetGreen shall be the sole and exclusive scheduled air carrier providing service under this block hour or passenger revenue guarantee in whatever direct or indirect form between OPR and LGA. The cash inducement would be paid from airport revenue.

Accept above offer from JetGreen Airways but the cash inducement would be paid out of the city's general fund and contributions from neighboring counties.

Which option(s) would be consistent with the FAA's revenue use policy? Besides the financial arrangement, is there any other issue that airport management should inquire about?

Hypothetical No. 8

PFC

Bono Regional Airport has just learned that two of its air carrier tenants has declared bankruptcy. Bono has a \$3 PFC and depends upon this revenue stream for its new round of airport development. The following two months, airport management notice that they have not received the monthly PFC checks from the two air carriers. It appears that the carriers have ceased payment of the PFCs paid to them by their passengers. Airport management calls up the carriers and is advised that they have no funds with which to pay the PFCs. What can airport management do?

Hypothetical No. 9

Exclusive Use Lease

Airport X obtains authority from the FAA to collect and use PFC revenue to construct new gates and baggage facilities. Recluse Airways approaches the airport with an offer to lease the new PFC-funded gates for 6 years on an exclusive use basis but at double the usual rent. Do PFC rules permit the airport to accept the carrier's offer?

Hypothetical No. 10

Access Roads

Airport X desires to increase efficiency of vehicular traffic flow into and out of the airport. Airport X's city government decides to build a new access road from a nearby interstate highway to the airport. Between the interstate and the airport will be three major intersections. The city manager reminds the airport manager how tight things are and encourages the airport to cozy up to the local FAA airport district office and find out how to maximize use of FAA AIP grant funds for this roadway project. What types of Federal funding would be available to pay for this project? What parts of this access highway, including the intersections, may be paid for out of AIP or PFC? How much would the local match be? The city's civil engineer advises that 97% of the traffic using the first intersection will go the airport, 64% of the traffic using the next intersection would go the airport, and 14% of the traffic using the last intersection (before the access road connects with the interstate) would go the airport.

Hypothetical No. 11

Terminal Upgrading

Airport Y desires to renovate and upgrade its overused terminal which has not been renovated since 1967. To what extent could the airport use AIP (discretionary) or PFC for the upgrade?



Hypothetical No. 12

Weekend Flyer Airport

Weekend Flyer Airport, a medium sized GA facility, wants to use non-primary AIP entitlement monies to pay for badly needed revenue producing facilities. Its two runways are a bit shabby and there patch work is needed in several taxiways and aprons. May the airport use its entitlements to build a sporty new hangar to attract corporate jets (\$\$)? If the airport gets to use the entitlements for the hangar, how much would the local match be?

Hypothetical No. 13

Airport Beautification

Monet Regional Airport (medium hub) decides it needs to undergo some beautification to be competitive with a new air carrier airport located 50 miles away. Monet airport management apply to the FAA to use their AIP entitlements to pay for aviation artwork and copies of famous Impressionistic works to upgrade the dingy terminal. They also request grant funds for decorative landscaping (will also help with community acceptance of the airport) throughout the airport grounds, and to construct a car rental facility. Would these projects be AIP and/or PFC eligible?

Hypothetical No. 14

Terrorist Threat at GA Airport

Suspicious individuals are observed lurking about a small GA airport within 100 miles of Washington, D.C., peeking in airplanes and taking photographs. Airport management quickly decide that they need to install security fencing with barbed wire around the perimeter of the airport. As of right now, there are no such access controls. The airport contacts the Washington Airports District Office and begs for an AIP grant to pay for the security fencing. The airport writes a letter to their U.S. senator for assistance in obtaining the grant. What result?

Hypothetical No. 15

City Park

An airport sponsor is sued by an environmental organization for contaminating a lake with aircraft deicing fluids. The settlement agreement calls for the sponsor to restore the area as a park and outdoor education center and to pay for ongoing operating and maintenance costs (for 20 years). The airport closes and the sponsor transfers the property to the city parks department. Can the sponsor continue to make all of its remaining payments under the settlement agreement without violating the revenue diversion standards?

Hypothetical No. 16

Truth or Consequences

International

T&C airport, mainly a GA airport but having some commercial passenger service, maintains a monopoly over the sale of jet fuel. It derives a significant percentage of its revenue from this activity. It allows FBO Center, an FBO, to self-fuel its own aircraft. FBO has now asked to fuel its subtenants as well. Can T&C maintain its exclusive fueling? Can it do so while allowing FBO to fuel its subtenants? If it does allow FBO to do so, can it reassert an exclusive fueling program?