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# THE IMPACT OF AIRLINE-AIRPORT RELATIONS ON AIRPORT MANAGEMENT DECISIONS

Dayl Arlene Cohen

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# ABSTRACT

Airlines, in the past, have had an important influence on airport operations through privileges granted them by the airport lease agreements. Airport administrators and sponsoring agencies have agreed to grant these privileges because much of airport capital investment has been amortized with airline money. This has been accomplished through the mechanism of the long-term lease.

This paper examines the working relationships which have been developing between airlines and airports in recent years. These relations have been influenced by deregulation and by inadequate airport capacity--both actual and anticipated--for growing passenger demand. Through an examination of the current role that airlines play in obtaining capital financing for airports, and an analysis of the leases and use agreements between airlines and three U.S. airports, a consideration of the diverging priorities of airports and airlines is presented.

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TABLE OF CONTENTS

Abstract..............................................2

Acknowledgements......................................3

ONE: U.S. Airports Today..............................5

TWO: Financing Airports Throught the Bond Market......15

THREE: Airport Leases and Use Agreements..............47

FOUR: Atlanta-Hartsfield International Airport........73

FIVE: Kansas City International Airport...............94

SIX: Boston-Logan International Airport...............114

SEVEN: Conclusion.....................................138

References............................................143

Bibliography..........................................149

Appendices............................................153

# CHAPTER ONE: U.S. AIRPORTS TODAY

Three thousand, two hundred and three (3,203) of the nation's 15,000 airports and airstrips are public-use airports, equipped with at least one paved and lighted runway. Of these, more than 83% (2,600) are exclusively general-aviation airports. The remaining 560 have scheduled service by major airlines, commuters, and/or air taxis. Two percent of all public airports--the seventy-one largest-- serve almost 90% of the nation's air passenger traffic.

Larger commercial airports in the United States are usually publicly owned at the local level--either by state, municipality, county, or public authority. A typical municipally-operated airport is city-owned and run as a department of the city. Policy direction comes from the city council and/or a separate airport commission or advisory board. County-run airports have a similar organization. Airport investment decisions are generally made within the context of city- or county-wide public investment needs and goals.

Some commercial airports are run by port authorities, which are legally chartered with the status of public corporations and operate a variety of publicly-owned facilities, such as harbors, bridges, tunnels, toll roads and airports. Port authorities have extensive independence from state and local government, which is founded upon their ability to issue their own debt and to control their own operating revenues. Some port authorities also have the power to tax within the port districts.

Aviation or airport authorities are similar in structure to port authorities, except that they have, as their single purpose, operation of an airport. They can also issue their own debt, and they operate upon the financial base of their own revenues. This base, however, is

solely derived from the airport and is, therefore, much narrower than that of a port authority.

State-run airports are managed by state departments of transportation. They raise capital investment funds through use of bonds, and a state tax on aviation fuel is sometimes another source. Of the nation's large- to medium-sized airports, only some of those in Alaska, Connecticut, Hawaii and Maryland are state-run.

Finally, the FAA operates two commercial airports in or near the District of Columbia: Washington National and Dulles International. Capital development of these two is financed through Congressional appropriations, and project costs are recouped from airport revenues.

Airport size categories are based upon percentages of total passenger enplanements per year. Large airports handle one percent or more of all yearly passenger enplanements in the U. S. (an enplanement refers to an entire through trip, but any connections constitute an additional enplanement). From 1982 data, twenty-four airports are categorized as large. Medium-sized airports handle between 0.25% and one percent of all enplanements. This category includes 489 airports. The final category is general-aviation airports, which serve non-scheduled, private air-traffic. There are 2,643 general-aviation airports across the country.

The aviation industry has, of course, experienced tremendous changes since the passage of the Deregulation Act of 1978. These changes have impacted upon airports as much as airlines. As early as 1979 R. G. Glumack, Executive Director of the Minneapolis-St. Paul Metropolitan Airports Commission, anticipated the major changes that airports would experience:

> (1) Airport financing will become more complex because of the changing nature of the security that supports airport revenue bond financing.

(2) Air service management and coordination will become the direct responsibility of the airport sponsor. The sponsor will have to solve problems of air service deficiencies and unproductive service without the benefit of C.A.B. [Civil Aeronautics Board] regulation.
(3) Airport capacity, if not already saturated, will soon become saturated. Dramatic increases in the number of airlines serving a market, and in the number of aircraft, people, and cars at airports are currently overwhelming the airside, landside, and environmental capacities of many airports.[1]

All three of these predictions have proven true--at least for some airports--and they will appear as underlying themes throughout this study.

The major influence that deregulation has had upon the industry--including airports--is that it has created a climate of constant fluctuation. Airlines enter and abandon markets at will and reconfigure their route structures with an equal lack of constraints. New carriers enter the industry and, of course, new and old carriers go bankrupt. This situation, even if it is beginning to moderate, somewhat, has inevitably affected the traditional relationship between airlines and airports. This is due to the fact that more airlines exist to be accommodated, while no new airports have been built, and expansion, for many existing airports, is limited. Also, the absence of the stability formerly supplied by the C.A.B. has increased the burden on airport management in planning for an uncertain future and in operating in a variable present.

Another consequence of deregulation, and the primary reason for significant increases in traffic at some airports, is the growth of the "hub" airport phenomenon. As airlines have restructured their routing networks, operations at airports chosen as hubs have grown tremendously. This is due to two influences: (i) the hubbing carriers

concentrate a great number of flights at these central points in their networks, and (ii) commuter airlines and air taxis are attracted to hubs in great numbers because they offer more opportunities for travellers from small communities (the typical commuter passenger) to connect to the national air transport system. The logical outcome, of course, is greater diversity of traffic at these airports, both in aircraft types and types of passengers.[2]

Another characteristic of hubs is that, once established, they create their own momentum. One airline creates a hub at a certain airport, and others then come to take advantage of the increased passenger activity and the possible "feed" of passengers from other hubbing airlines. As hubs develop, internal transfer of passengers and baggage becomes extremely important. The airlines are generally the ones who finance the necessary improvements to facilitate this movement, thereby reducing their mobility and increasing their commitment to the hub.[3]

The trend toward hubbing since deregulation has brought large amounts of new traffic to some airports (while reducing it at others), but may prove to be a mixed blessing. If an airport makes a large capital investment to accommodate a carrier wishing to establish a hub, it may find itself in financial difficulties if the carrier changes its plans or goes bankrupt.

Other problems for airports are cited by David W. Davis, Executive Director of the Massachusetts Port Authority (Massport), in testimony before the House Subcommittee on Aviation, in August, 1979:

> Deregulation is creating new pressures on existing problems and, if not resolved in time, they could very well defeat the purpose of deregulation. Mr. Chairman, unless some direct attention is given to efficient use of both airspace and landside capacity and noise control, I fear that we will be faced with some very serious problems. It

> now appears that deregulation will mean fewer long distance non-stop flights for smaller and medium-sized cities, accelerating the hub-spoke system to large hub airports practiced by many airlines. Many of the larger airports are already operating at or very near finite capacity limitations. The increasing volume of commuter aircraft combined with new air carrier service are forcing airport operators to contemplate hard choices in order to prevent congestion at their airports from proliferation of services.[4]

Another emerging trend is that some airports are finding it necessary to compete for traffic. This is especially true of those which do not have a naturally large amount of origin-destination traffic. Areas such as the Midwest, therefore, are filled with airports which could become hubs for the carriers. The result is that marketing has become a much more important component of airport management than ever before.

Changes such as these have created a growing emphasis on the ability to be flexible among airport authorities, in recent years, and airport operators are reevaluating their relationships with the airlines. T. James Truby, state aviation administrator of Maryland, has been quoted:

> I think what we're seeing is that airport operators are pushing more aggressively for a more equivalent relationship with the carriers. . . . There is strong interest now on the part of airport operators to take control of their airports and make decisions that are in the best interests of communities served by the airport.[5]

Some of the factors which can affect the airline - airport business relationship are:

(1) airline guarantees of airport revenue bonds,

(2) the airport sponsor's policies and goals,

(3) who is defined as the constituency of the airport: airlines, air travellers, the community, the region, etc.,

(4) present constraints regarding airfield or terminal capacity,

(5) the airport's options regarding future expansion of capacity.

One of the focal points of the airline-airport relationship is the setting of fees and rentals for the airline's use of the airport. This is an area in which airlines have traditionally had strong influence, and some airport operators are reevaluating the airlines' role. In a study for the Federal Aviation Administration (FAA) in 1984, the major considerations for an airport in defining a rate-setting approach were suggested to be:[6]

(1) the definition of recoverable costs - The variables include such factors as (i) maintenance and operations (M&O), (ii) the allocation of overhead and administrative costs, (iii) capital costs such as debt service coverage and interest, (iv) the basis for setting the period of amortization of debt, (v) credits and charges from prior years, (vi) recovery of investments in land;

(2) the definition of rentable space;

(3) allocation of revenues and costs to airport cost centers;

(4) allocation of the costs of commonly-used and jointly-used space (more than one airline uses the space, but it is not considered "public" area);

(5) whether rental rates are averaged over all equivalent space, or differential rates are established to reflect actual costs of construction and operation of each area.

The airport operator must also define its policy regarding profits: should the airport be profit-making or merely attempt to

break even? Items such as depreciation and reserve funds must be defined as either profits or costs, and the question of whether excess operating revenues should be accumulated for funding future projects or credited to user fees and rental rates must be answered.

This financial relationship between airports and airlines in the U. S. today can be broken down into two general categories:

(1) the residual-cost approach, in which the airlines assume much of the financial risk by agreeing to pay any costs of running the airport that are not covered by other sources of revenue.

(2) the compensatory approach, in which the airport operator assumes the major financial risk and charges user fees and rental rates so as to recover the actual costs of the facilities.

There are varying application of the residual-cost approach, but, in general, it works in the following manner: the total annual costs, including administration, operations, debt service, etc., are calculated for each cost center (e. g. terminal, airfield, service roads, freight areas). These are offset by non-airline revenues anticipated for that center. The residual between costs and non-airline revenues then provides the basis for use of facilities within the cost center. Any surplus is credited to the airlines, and any deficit is charged to them in calculating the rates, which then apply in the following year. The rates paid by the airlines, then, are probably unequal to the actual costs of the facilities they use.

Under a compensatory approach, airlines pay rates equal to the costs of the facilities they use, as determined by cost accounting. The airlines at such airports, then, provide no guarantees that airport revenues will suffice to cover annual operating and debt-service requirements.

In this approach, the annual expense of running each cost center is calculated, and the airlines' shares of these costs is based upon their actual use of facilities. The airlines are not charged for public space, such as terminal lobbies, nor do they receive credit for non-airline revenues.

In the 1984 study for the FAA, a survey was done of several U. S. airports in order to catalogue the various approaches taken to airport rate-setting. The following practices were found:[7]

(1) Landing fees:

(a) compensatory - airfield costs are allocated among users, usually on the basis of landed weight. The resulting rate per measure of landed weight (or take-off weight) is calculated to "compensate" for all costs assigned to the airfield.

(b) cost center residual - airfield costs are credited with revenues from non-airline airfield use (e. g. fuel flowage fees), and the residual amount is divided by landed weight to determine the landing fee rate.

(c) airport residual - total airport costs are reduced by the amount of revenue from all sources other than landing fees, and the residual amount is divided by landed weight to determine the landing fee. The "costs" included usually include such items as debt-service coverage and/or airport discretionary funds, etc.

(2) Terminal building rents:

(a) compensatory - terminal building costs are allocated to sub-cost centers. The costs allocable to airlines are then divided by the area of airline space to determine

the average rental rate. The airlines do not pay for any costs of public or common-use areas of the terminal, and the airport operator assumes the risk of generating enough concession, etc. revenue to cover these costs.

(b) modified compensatory - total terminal building costs are divided by total square footage of usable space to determine average rental rate. Once again, the rate does not include costs of common-use areas. A variation of this method obligates some airlines to make additional payments to cover any shortfall of concession revenues. These are reimbursed in future years from any available excess concession revenue.

(c) "cost-of-service" compensatory - total terminal costs are divided by the total rentable space in the building. Costs of public or common-use space are included in the calculation. Concession revenues in excess of the allocated cost of concession space are retained by the airport for discretionary use.

(d) cost center residual - total terminal costs are reduced by the amount of non-airline revenue, and the residual amount is divided by the total square footage of airline rentable space to determine the average rental rate.

(e) appraisal - establish rental rates on the basis of a commercial appraisal of the space.

Airports and airlines have traditionally opted to formalize these arrangements in lease agreements or lease and use agreements, and this fact makes these documents useful in examining current developments in the airline - airport relationship. The most noticeable trend in the lease agreements covered in this study is the strong evidence that many

airport sponsors no longer regard the air carriers as their primary constituency. During the pioneer days, close cooperation between airline and airport was necessary, simply in order to build an air transportation system. Later, during the boom years, it appeared that the best way of accommodating the air traveler and strengthening the air transport system was to first meet the needs of the carriers. Today the air traveler is still of primary importance, but the local constituency often takes precedence over the requirements of the carriers. This trend is reflected, to some extent, even in leases that appear to be more traditional, as we shall see.

## CHAPTER TWO: FINANCING AIRPORTS THROUGH THE BOND MARKET

The issue of financing airport capital expenditures has been reexamined in recent years as major changes in the aviation industry have taken place. Airline deregulation has caused the shape of the nation's route networks to change drastically and to be more fluid than anyone would have thought possible only ten years ago. Since airports are the origin-destination points of these networks, the changes have had a profound effect upon them. In the midst of this, the Federal Government has been reassessing its role in financing airports with Federal aid. More attention is being focused upon the private sector, in particular the municipal bond market, as a source of capital funding for airports. The private market, however, has its own requirements for potential borrowers, and exerts its own influence upon airports, their management, and their relationships with the airlines that serve them. An example of airport financing, then, especially from the bond market, can provide useful insights into the issues that airports are currently facing.

Capital improvement of airports can be financed in a variety of ways: federal grants, local and state government financing, and the commercial bond market, as well as accumulated surpluses from airport revenues. Civil airports were financed by municipal and private agencies up until the early 1930's. Between 1933 and the beginning of World War II, Federally-sponsored public relief programs provided over 385 million dollars to airport development.

After World War II, the enactment of the Federal Airport Act made funding available for airports under the Federal Aid Airport Program (FAAP), in recognition of the fact that an adequate system of airports was a matter of national concern. The program offered matching funds

of 50% to 94% for capital expansion an rehabilitation of airports. The Act remained in force until 1969 and provided 1.2 billion dollars in federal funds. The amount spent was unable to keep pace with industry expansion, however, and this fact led to the Airport and Airway Trust Fund.

Taxes on on ticket sales and general aviation fuel, .which had been established in 1933 and 1941, were formally linked to airport expenditures by this act. In addition to the eight per cent tax on ticket sales, a tax of fourteen cents per gallon on general aviation jet fuel and twelve cents per gallon on avgas contributes five percent of trust fund revenues. The 1970 Act provided 2.5 billion dollars for airport improvements and development, over the next ten years, to airports included in the National Airport System Plan. The 1970 Act expired on June 30, 1980, and was replaced by the Airport and Airways System Development Act of 1979.

The amount of the matching grants which are disbursed through the trust fund are determined by a formula based upon passenger volume or through discretionary grants for special needs. Federal aid to airports is expected to increase from 400 million dollars in 1982 to 800 million dollars in 1986 (in 1982 dollars). Between 1960 and 1982, the Federal share of cumulative public and private investment in airports amounted to just over one-third of the 25.1 billion dollar total. The state's share in airport investment has maintained a fairly stable eleven percent since 1970.[1]

At the local level, airport funding has come primarily from the general taxes of the local government which owns the airport, and from the commercial bond market, through the sale of general obligation bonds and revenue bonds. General taxation was the most common source in the early years of aviation, but has proved to be impractical and

inadequate as capital requirements for airport development have grown. The result is that more and more airports have looked to the municipalbond market as a source of funding. Many major commercial airports have been able to attract investment dollars from the private marketplace in the form of these tax-exempt bonds. These airports have had to demonstrate sound financial performance in order to compete for private-sector funds, and they have done so quite successfully.

## The Airport Bond Market

Airport bonds are included in the general class of municipal bonds, a term used to describe all bonds issued by governmental entities, except for Federal government bonds. Two major types of financial backing are used to secure municipal bonds:

(1) general obligation bonds pledge the unlimited taxing power and full faith and credit of the government body issuing them;

(2) revenue bonds pledge the revenues, in this case, of the entire airport, or of the specific facility to be developed

General obligation bonds can obviously only be issued by governmental bodies with taxing powers, such as states and municipalities. Most states limit the amount of total general obligation debt that a municipality may issue, and many states require voter approval before any general obligation debt can be issued. These limitations are not true of revenue bonds.

Revenue bonds, on the other hand, usually have higher interest costs than general obligation bonds, due to the fact that they are backed by receipts from user charges, which are subject to greater

uncertainty than are taxes. In the 1978-82 period, revenue bonds represented nearly ninety-two percent of the total dollar volume of airport bond sales.[2]

General obligation bonds can be issued at a lower interest rate than the prevailing rate for municipals, and no coverage (assets available to cover the liability of the bond issue, usually in a specified ratio to the amount of the debt) is required. Interest from general obligation municipal bonds is exempted from federal income taxes.

General obligation bonds were once widely used for airport financing, but, from the airport management's point of view, they involved undesirable restrictions--for one, a legal limitation on total general obligation liability usually existed--often five percent to ten percent of the valuation of the taxable property of the issuing body. General obligation bonds often had other strict statutory requirements, such as the need for voter approval and a shorter retirement period for the bond.

A newer generation of "self-liquidating" general obligation bonds has different characteristics which can circumvent these problems. Repayment is secured by the issuing government body, but payments are actually met by revenues generated by the operation of the airport. Further, the debt is not considered part of the community's debt limitation, making these bonds more attractive to community and airport, alike.

Larger airports use relatively little general obligation financing, especially where investments are large and where revenues from airport operations are sufficient to cover debt service requirements. This keeps airport capital expansion from placing too heavy a burden on municipal debt and reserves this source of financing

for municipal projects which cannot cover the costs of debt with their own revenues.

These airports rely on airport revenue bonds, the debt service on which is payable solely from the revenues derived from the operation of the airport or from the facility on the airport which was specifically funded by the bond issue. These bonds are also classified as municipals, therefore interest earned from them is also exempted from Federal income taxes.

Airport revenue bonds can be found in several variations. Included among them are:

(1) Traditional revenue bonds, also known as deficit financing, have debt service guarantee from the airlines, which also sign long-term leases with the airport owner. The airlines pledge to pay higher landing fees should airport income fall short of the total needed to pay off the principal and interest on the bonds.

(2) "Gross pledge" bonds are those in which the gross revenues of the funded project are first pledged to the payment of debt service on the bonds, and, thereafter, to use in maintenance and operations of the facility.

(3) Leases bonds, also know as "special facilities" bonds, are secured solely by the rentals derived from a lease instrument between airport owner and users of the funded facility.

(4) Serial bonds are bonds of one issue which do not all mature on the same date. Rather, they mature at a staggered rate, so that some portions of the issue come due before others. Sometimes they also contain call

options, enabling the airport to "call" the bond and settle the debt before the maturity date.[3]

Revenue bonds will usually contain several covenants (restrictions and requirements) designed to assure the purchaser that the investment will be safeguarded. These will pertain to accounting and fee setting practices, restrictions on further indebtedness, promises to maintain the enterprise so as not to reduce its value, etc.

Airport revenue bonds are generally repaid through a sinking fund (a fund established to retire debt before maturity), a bond fund, or by serial withdrawal. Rarely, repayment is made at maturity either by current revenues or by refunding through a sale of new issues. Refunding bonds are also sometimes issued to restructure the debt of older issues and release the airport from the obligations of the older issues. Many airports also have bond reserve funds in case the sinking fund or bond fund falls short.

The process of marketing a bond issue is as follows: the airport issuing the debt will generally sell its entire bond issue to investors. The dealer, or syndicate of dealers, is known as the underwriter. In the case of municipal offerings, underwriters are often chosen through competitive bids. The airport and the underwriter reach agreement over what interest rate the bonds shall bear. The underwriter then prices the bonds for general sale so as to make a profit. The ideal interest rate will be set to incur the lowest interest cost to the airport along with the greatest return on the resale of the bonds.

Bonds are described in terms of either price (usually expressed as a percentage of the face value) or yield (average rate of return once the difference between buying price and face value is taken into account). Prices and yield rates move inversely to one another. In

deciding the price of a particular bond issue, underwriters will first identify a range of interest rates on the basis of market conditionsand then specify a rate based on the credit of the enterprise in question. General market conditions represent the most important determinant of rates on airport revenue bonds, thus giving airports little control over their cost of capital. Statistical analysis indicates that each one percent change in the overall market rate for municipals leads to roughly a one percent change in the rate for airport bonds.[4]

In the process of redefining the general market rate for an individual airport, two factors have greatest importance. The first is the airport's fiscal condition, including its prospects for traffic growth and the status of its local economic base. The second is the presence of pressures on the airport to expand capacity, necessitating extensive capital investment and increased debt.[5]

Airport revenue bonds, for the most part, receive bond rating from either Moody's Investors Service, Inc. or Standard and Poor's Corporation (see accompanying tables). The relative investment quality of bonds is rated by a gradation system which classes the bonds from lowest risk down to highest risk. Bond ratings are revised as changes in the financial position of an enterprise are perceived by the market. It should be noted, however, that ratings do not cause bond prices to rise or fall on the market. The same information which investment services use to determine the rating is being independently assessed by underwriters (for a new issue) and by brokers and prospective buyers in the secondary bond market. The bond rating, rather than determining the marketplace's assessment, is a shorthand indicator of what that assessment is. A bond's price on the market may change well before a rating revision. Today's market pages in the newspaper, therefore, may contain more information about an enterprise's investment value than the bond rating does.[6]

TABLE 2 - 1: MOODY'S BOND RATINGS

**Aaa**

Bonds which are rated Aaa are judged to be of the best quality. They carry the smallest degree of investment risk and are generally referred to as "gilt edge." Interest payments are protected by a large or by an exceptionally stable margin and principal is secure. While the various protective elements are likely to change, such changes as can be visualized are most unlikely to impair the fundamentally strong position of such issues.

**Aa**

Bonds which are rated Aa are judged to be of high quality by all standards. Together with the Aaa group they comprise what are generally known as high grade bonds. They are rated lower than the best bonds because margins of protection may not be as large as in Aaa securities or fluctuation of protective elements may be of greater amplitude or there may be other elements present which make the long term risks appear somewhat larger than in Aaa securities.

**A**

Bonds which are rated A possess many favorable investment attributes and are to be considered as upper medium grade obligations. Factors giving security to principal and interest are considered adequate but elements may be present which suggest a susceptibility to impairment sometime in the future.

**Baa**

Bonds which are rated Baa are considered as medium grade obligations, i.e., they are neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such bonds lack outstanding investment characteristics and in fact have speculative characteristics as well.

**Ba**

Bonds which are rated Ba are judged to have speculative elements; their future cannot be considered as well assured. Often the protection of interest and principal payments may be very moderate and thereby not well safeguarded during both good and bad times over the future. Uncertainty of position characterizes bonds in this class.

**B**

Bonds which are rated B generally lack characteristics of the desirable investment. Assurance of interest and principal payments or of maintenance of other terms of the contract over any long period of time may be small.

**Caa**

Bonds which are rated Caa are of poor standing. Such issues may be in default or there may be present elements of danger with respect to principal or interest.

**Ca**

Bonds which are rated Ca represent obligations which are speculative in a high degree. Such issues are often in default or have other marked shortcomings.

**C**

Bonds which are rated C are the lowest rated class of bonds and issues so rated can be regarded as having extremely poor prospects of ever attaining any real investment standing.

Source: *Moody's Industrial Manual, 1979.*

TABLE 2 - 2: STANDARD AND POOR'S BOND RATINGS

**AAA**

This is the highest rating assigned by Standard and Poor's to a debt obligation and indicates an extremely strong capacity to pay principal and interest.

**AA**

Bonds rated AA also qualify as high-quality debt obligations. Capacity to pay principal and interest is very strong, and in the majority of instances they differ from AAA issues only in small degree.

**A**

Bonds rated A have a strong capacity to pay principal and interest, although they are somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions.

**BBB**

Bonds rated BBB are regarded as having an adequate capacity to pay principal and interest. Whereas they normally exhibit adequate protection parameters, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity to pay principal and interest for bonds in this category than for bonds in the A category.

**BB B CCC CC**

Bonds rated BB, B, CCC and CC are regarded, on balance, as predominantly speculative with respect to the issuer's capacity to pay interest and repay principal in accordance with the terms of the obligation. BB indicates the lowest degree of speculation and CC the highest degree of speculation. While such bonds will likely have some quality and protective characteristics, these are outweighed by large uncertainties or major risk exposures to adverse conditions.

**C**

The rating C is reserved for income bonds on which no interest is being paid.

**D**

Bonds rated D are in default, and payment of principal and/or interest is in arrears.

Source: *Standard and Poor's Bond Rating Definitions* (1977).

In April of 1984, a study of airport financing was published by the Congressional Budget Office (CBO). Their research indicated three conventional gauges of investment quality, each with particular implications for airport bonds:[7]

(1) Bond ratings--Not all bonds are rated, but airport bonds which receive ratings do well, varying between top and medium grades. General obligation bonds draw the best ratings, the rating being determined by the economic strength of the entire state or municipality.

In establishing ratings, credit analysts consider factors such as the overall financial performance of the airport, the strength of passenger demand, and lease agreements with the airlines serving the airport. In particular, passenger demand is an important factor in financial strength, and special attention is paid to past and projected passenger growth. Growth is considered critical because capital investment must be accompanied by growth in airport use, or the project will dilute the airport's ability to repay its outstanding bonds. Other factors considered important are types of air transport service, numbers of air carriers, air carrier market share, and diversity of revenue sources, which last is thought to add stability to the airport's income stream.

Airline deregulation has caused a shift in the emphasis given to these factors. In particular, the credit analysts tend to view strength of local economic conditions as having more importance than lease agreements or the financial stability of the airlines serving the airport. It is felt that if one airline fails or withdraws from service to a city, a strong local economy could attract other airlines to fill its place. For example, the following statement appears in the Standard and Poor's Ratings Guide of 1979:

> Although most airports rely to a large extent upon the rental payments and landing fees paid by the airlines utilizing the facilities, in most cases we do not examine the creditworthiness of the airlines serving the airport. Instead, we make the assumption that if there is demand for an airport and an airline that has historically served the airport is not able to continue for some reason, then another airline will pick up the slack. As a result, our analysis focuses on the demand for the facility as well as its legal and financial structure.[8]

Diversity of revenue sources and the ability to raise revenue in other areas, such as concessions and parking facilities, are also cited as considerations. Lastly, debt service coverage, facility utilization versus capacity, management of costs and budget, and airport-airline working relations are specifically mentioned as important factors in determining a rating.

With the importance attached to passenger traffic and a strong financial base, it is not surprising to find that large airports receive the highest ratings. Over the period 1978-1982, not one large airport that issued debt was rated below the upper medium category.

Growth alone does not guarantee an improved rating, however. The airports that have experienced the greatest operational growth also have the greatest need for extensive capital expansion, along with like increases in debt financing. At Chicago's O'Hare Airport, for example, "the magnitude of the capital program being undertaken at the airport" has kept Standard and Poor's from raising the rating on its most recent bond issue above an A.[9]

(2) Interest costs--This second standard gauge of a bond's investment quality is an indicator that airports hold a strong position in the municipal bond market. This is shown by the generally lower interest costs paid by them in comparison with other public enterprises.

The CBO study noted that an airport's fiscal condition seemed to be more important in determining interest rates than the existence of long-term use agreements with airlines. Airport size (or traffic volume) also has an effect upon interest rates, with "elasticity" of interest cost with respect to airport size averaging -0.013 over the period 1978-1982. In other words, an airport with ten percent more passenger boardings than another airport would pay interest rates about 0.13% lower on its bonds. A pattern did appear, however, of large airports incurring somewhat higher interest costs than small airports, and medium-sized airports paying higher costs than either.

Two factors figure in this pattern. First, the market is cautious about expensive expansion with its accompanying increase in the ratio of debt to total assets, implying a decrease in revenues available to service already outstanding debt. Second, the size of an issue for a large airport is much greater than that for a smaller airport, and underwriters usually charge a premium in such cases to cover the added risks of marketing such a large number of bonds. These factors can offset the moderate advantage of slightly higher ratings.

(3) Defaults--An enterprise's default history is the third common gauge of its investment value. Airports have a strong record in this area, having never suffered a single default.

Between 1978 and 1982, airports raised a total of five billion dollars (1982 dollars) on the bond market. By far the majority of this was in tax-exempt municipal bonds. Larger airports were more active in this market for funds, with 58% of the large and medium-sized airports using bond financing in this period. In dollar volumes, 89% of municipal debt sold for airports was for large and medium-sized airports. Finally, airport investment dollars raised through the bond

market exceeded Federal grants to large airports by 340%, while at small airports, Federal grants were more than double the funds from bonds.[10]

Airlines and Airport Financial Management

In the preceding discussion of revenue bonds, the role that the airlines play in airport financing was an emerging theme. In addition to their formalized structures of management, airports are operated in conjunction with a private industry: the airlines. They, therefore, have both a public and a private character which give all of their management practices a distinctive shape--including, and often especially, their financial management practices. The CBO study surveyed sixty of the nation's large and medium-sized airports and found that a slight majority of them have some form of residual-cost approach to financial management (as described in the previous chapter), while the rest--42%--of the airports surveyed are currently using a compensatory approach.

The differences between these two approaches have significant implications for airport financing. In particular, three factors are affected:[11]

(1) Retention of earnings--The availability of substantial revenues in excess of costs can strengthen an airport's performance in the bond market. Residual-cost financing guarantees that an airport will always break even, but it precludes, by definition, an airport's generating substantial earnings in excess of costs. On the other hand, an airport managed under the compensatory approach is not guaranteed to break even. It can, however, do better than break even and retain a substantial surplus. The extent of such a surplus will generally

depend upon the level of non-airline revenues which can be generated. Airports with a compensatory financial approach do tend to have a stronger fiscal performance. The study found that they drew interest rates that were ninety-five basis points below other revenue bonds over the 1978-82 period. Residual-cost airports paid only four basis points below other municipals (a basis point equals one one-hundredth of a percentage point.)

A few residual-cost airports have modified the approach to enable them to retain earnings usable for capital development. This is done by excluding some revenues from the base used in calculating the residual cost to the airlines. These revenues are directed into a discretionary fund that can finance capital projects.

It should be noted, however, that controversy surrounds the issue of how much retained earnings a publicly owned airport should accrue. On September 30, 1982, a U.S. District Court judge found against Indianapolis Airport in its suit against six resident airlines: American, Delta, Eastern, Ozark, TWA, and US Air. The judge stated, "It is obvious plaintiff's [the airport's] method [of financial management] is intended to produce revenues substantially in excess of the cost of operating the facility."[12]

Indianapolis Airport had raised its fees and, at the same time, had formed plans to build a new terminal building and a new runway, which expansion was objected to by the airlines serving the airport. In court, the airlines argued against the higher rates and the airport's retention of concession revenues rather than using them to reduce airline payments. Their objection to the expansion plans was apparently at the heart of their resistance. They were concerned about having to pay for what would be an overbuilt facility, as demand for travel to Indianapolis was decreasing. The airport, on the other hand,

had seen the issue as one of whether or not it had the power to set its own fees and to determine the use of its own revenues.

(2) Majority-in-interest (MII) clauses--This second factor in airport financial management is found more commonly as a feature of use agreements at residual-cost airports than at compensatory airports. In the CBO survey, 71% of residual-cost airports had such a clause, while only 24% of compensatory airports did.

MII clauses give the airlines which comprise a majority of an airport's traffic the opportunity to approve or disapprove capital projects that would significantly increase the rates and fees the airlines would have to pay. The airlines assume a significant amount of financial responsibility for the airport under a residual-cost arrangement, and this type of clause affords them some protection.

Specific MII clauses vary widely in their provisions. At some airports, airlines have veto power over any project which will cost more than a specific amount, while at others projects can only be deferred for a time.

(3) Term of the lease agreement--Residual-cost airports typically have longer-term lease agreements than do compensatory airports. At residual-cost airports the agreements have typically been written with security for long-term revenue bonds in mind. The term of the agreement, with its airline guarantee of revenues for debt service, has often coincided with the term of the bond. Terms of thirty years are not uncommon.

The CBO study also examined trends in airport financial performance from 1978-1982. It used four indicators of financial health in its assessments. They were:[13]

(1) Operating ratio--This is derived by dividing operating expenses by operating revenue. A low operating ratio

indicates availability of funds for capital spending, after the ongoing operating expenses are covered.

(2) Net take-down ratio--This is calculated as total revenue minus operating expenses, divided by gross revenues. This includes non-operating revenues and is a slightly broader measure than the operating ratio.

(3) Debt-to-asset ratio--This is calculated as gross debt minus bond principal reserves, divided by net fixed assets plus working capital. Creditors prefer low debt-to-asset ratios because each dollar of debt is secured by more dollars of assets. The study does show, however, a general trend toward improved financial strength for airports, giving assurance that debt can be covered, despite the fact that airports tend to carry high levels of debt relative to the value of their assets.

(4) Debt service safety margin--This is calculated by gross revenues minus operating expenses and annual debt service, divided by gross revenues. This is a measure of percentage of revenues available to service new debt and of the financial cushion in the event of unexpectedly low revenues.

The accompanying table (Table 2-2) compares financial performance of airports by management approach. As the table makes clear, the three ratios that reflect gross revenues--operating ratio, net take-down ratio, and debt service safety margin--all show substantial differences between airports using the two different approaches. Compensatory airports show substantial strength over residual-cost airports.

FINANCIAL PERFORMANCE OF COMMERCIAL AIRPORTS COMPARED BY MANAGEMENT APPROACH, 1975-1982

| Performance Measure | Averages of All Airports in Category (In percents) | | | | | |
|---|---|---|---|---|---|---|
| | Residual Cost | | Compen-satory | | All Airports [a] | |
| | 1975-1978 | 1979-1982 | 1975-1978 | 1979-1982 | 1975-1978 | 1979-1982 |
| Operating Ratio | 56.2 | 52.9 | 52.5 | 44.3 | 54.5 | 50.2 |
| Net Take-Down Ratio | 46.5 | 51.5 | 53.2 | 60.8 | 48.5 | 54.2 |
| Debt-to-Asset Ratio | 40.4 | 55.3 | 47.3 | 40.5 | 39.0 | 48.1 |
| Debt Service Safety Margin | 16.0 | 24.6 | 33.1 | 48.3 | 19.9 | 31.6 |

SOURCE: Congressional Budget Office, based on financial performance data provided by Moody's Investors Service, Inc., for 13 large, ten medium-sized, and two small commercial airports.

a. Includes airports for which the management approach is unknown.

Source: Congressional Budget Office

Finally, the CBO study identified the major emerging trends in airport financial management. They are :[14]

(1) Shorter-term leases--The trend toward shorter-term lease agreements was in evidence before deregulation of the airlines and has continued since then. Short-term contracts give greater flexibility to adjust pricing and allocate space, as well as greater control over investment policies. More recent contracts may run for five years rather than thirty, or they may even be month-to-month operating agreements. Fifteen percent of the CBO-study airports have already instituted shorter-term agreements, and another twenty percent indicated plans to do so. Many shorter agreements, however, are due to the fact that no major capital development programs have been planned requiring long-term bond financing.

(2) Modification of the residual-cost approach--Several airports have introduced changes to their residual-cost approach to management. Examples are more compensatory approaches to calculating airline charges, weakening or eliminating of MII clauses, and provisions allowing for greater retention of earnings usable for capital development. Many airports have indicated a desire to move toward the compensatory approach as their long-term leases expire, although the court's decision in the Indianapolis case may have an adverse effect upon this trend.

The compensatory approach is attractive to airports which can develop strong markets and insure their revenue generating potential. They need not rely on the airlines, and they may adopt a compensatory approach to maximize revenues.

(3) Maximization of revenues--Airports are diversifying and maximizing revenues in a variety of ways. These include allowing for more frequent adjustment of user fees, using competitive bidding for

concession contracts, and exploring new sources of income such as video-game rooms and industrial parks on airport property. These trends indicate a growing search by airports for a stable stream of income which is less dependent upon airline guarantees.

In summary, differences in financial management approaches seem to indicate differences in earning power and financial strength. Gross revenue at compensatory airports depends mainly on volumes of passenger traffic, while gross revenue at a residual-cost airport may be constrained to the minimum amount to cover operations, debt service, and reserves. This may have serious implications for the availability of financing from the private sector.

## Airport Financing Before and After Deregulation

In the 1950's the bond financing for O'Hare International Airport was the beginning of what came to be the prevalent practice. The airlines pledged that, if airport income fell short of that needed to repay principal and interest on the bond issue, they would make up the difference through higher landing fees.[15] The O'Hare agreement with airlines demonstrated that airports need not depend upon tax funds to raise capital in financial markets.

The continuation of this practice into the 1970's is shown by an article which appeared the Air Transport Association's Air Transport Report in 1972:

> In recent years, the good credit of the U.S. scheduled airlines has become an extremely important factor in airport financing. Airports that need to raise money sell revenue bonds, promising to repay these bonds from the airport's earning. The airlines, in turn, guarantee that the airport's earnings--from the fees and rentals the airlines

pay—will be high enough to cover the principal and interest of the bonds, as well as maintenance expenses for the airport.[16]

A few years later a survey was done of airport revenue bond financing for large, medium, and small hub airports, as of 1977.[17] It showed:

(1) A majority of large and medium-sized airports were dependent upon revenue bond financing for capital improvement.

(2) Most of the airports were in good financial condition, as indicated by a bond coverage ratio between 1.25 and 1.50.

(3) The ratings by both Moody's and Standard and Poor's for a majority of large and medium-sized airports were A and above.

(4) A majority of airports which used revenue bond financing also had long-term use agreements with airlines, although only about fifty percent had agreements with terms extending through the entire term of revenue bonds.

(5) Out of twenty-five large airports, seven did not have debt service guarantee from airlines. Out of twenty-four medium-sized airports, eight did not have debt service guarantee from the airlines.

In the first years after deregulation, authors speculating upon the effects of this change upon airport financing argued that airports would have increased difficulty in attracting funds from the bond market and would have to pay more (i.e. higher interest rates) for this money. The reason given for this expected development was the greater uncertainty about the pattern of future air services.[18] One of the

consequences of the uncertainty which received particular attention was a demand for shorter lease terms at some airports by some airlines. It was felt that, without long-term agreements to act as tangible assurance of stable revenue streams, the bond market would become wary of airports. The airports hardest hit would, of course, be those most dependent upon the bond market for funds: the large airports that serve most of the nation's passenger traffic. However, beginnings of a trend in the bond market to accept airport revenue bonds with no debt service guarantee from the airlines, as well as no long-term leases, were in evidence even before deregulation. Bonds sold by San Francisco, Phoenix, and Las Vegas are examples.[19]

Since deregulation, as it has been noted, the bond rating services have emphasized that passengers, not airlines, are an airport's true clientele. Thus, "origin-destination" airports, where passengers either begin or end their journeys, in strong travel markets will have an advantage over the hub markets serving large numbers of transfer passengers. As an example, when Dallas-Ft. Worth Airport sold a bond issue in late 1982, it retained an A rating from both Moody's and Standard and Poor's, despite the collapse of Braniff Airways that year. Braniff was the dominant airline serving that area and had a large share of responsibility for airport revenues under DFW's residual-cost lease agreement. Moody's, however, stated that it took account of the airport's diversified revenue base and its role as a major facility serving the strong Southwestern economy.

In contrast, in May 1983, Moody's revised Atlanta's Hartsfield Airport down from A to Baal.[20] The reasons it gave were Eastern Airlines' financial troubles, along with a trend of declining traffic and reduced debt service coverage. Over 75% of Atlanta's traffic is made up of transfers, and Eastern user fees and rentals made up 41% of such airline revenues at Hartsfield.

Another trend since deregulation is that the financial performance measures of large and medium-sized airports have generally improved. It is plausible to speculate that this improvement may be at the expense of small airports which have lost air service, since 1978, to other more profitable routes. On the average, a ten percent increase in airport traffic will translate into a two percent improvement in those measures which are dependent upon gross revenues: operating and take-down ratios, and debt service safety margin. Increase in traffic, then, indicates improved gross revenues.

Increased business may also lead to a greater need for capital investment in expanded facilities, and this leads, in turn, to more debt. Medium-sized airports in particular have needed to expand their facilities, hence the increased average debt-to-asset ratio for airports in this class. This is a trend of some concern to credit analysts. The growing practice of concentrating operations at a few major hubs can eventually lead to increased borrowing costs and diminished access to private debt capital.

A further problem is that some existing lease contracts, especially the very long-term ones, can limit the amount of control that airport managers have over the structure and level of user fees and charges. This implies that the ultimate financial responsibility for airport development is not entirely in the hands of the airport managers. At those airports where MII clauses are employed, this is unquestionably true. The effect this can have on the cost of debt may be seen by the Standard and Poor's Corporation statement:

> In most cases the airlines have executed agreements with the airport which describe terminal rental payment and landing fees. These documents generally indicate an airport's flexibility in adjusting revenues collected from the airlines to meet financial shortfalls. A stronger credit

> will demonstrate the ability to change rates quickly and effectively to mitigate revenue shortfalls resulting from any number of causes.[21]

Deregulation, then, has not caused radical changes in the financial management of airports, but new trends, some of which had their beginnings in the years before deregulation, are emerging. Investors and analysts have increasingly recognized that an airport's financial stability depends more upon diversity of revenue sources, flexibility of contracts, and the strength of the local air traffic market than on long-term use agreements. Deregulation has underscored this fact by allowing airlines to leave an unprofitable market virtually at will. The shaky financial condition of many airlines, since deregulation, has also supported this point of view.

## The Example of Two Airports

An airport authority issuing a revenue bond series must be prepared to give out comprehensive data on the airport, the region, and the industry, as they pertain to the airport's ability to repay the debt. This is usually presented in the format of a prospectus, or Official Statement. The prospectus will contain complete information about the terms of the bond sale, an extensive description of the airport's financial situation, and background information about the aviation industry, the airport's operations, and its prospects. The prospectus will also describe the contract with bondholders, list covenants of the issuer, and state the rights and obligations of both issuer and bondholders. An examination of a prospectus, then, can yield a great deal of information about the airport's assumptions and expectations at the time the debt was issued.

A comparison of two Official Statements for recent airport bond issues, one by the Massachusetts Port Authority in 1984, and one by the City of Atlanta in 1982, will illustrate many of the actual effects of developments discussed in this paper. The discussion is not intended to be a detailed description of the contents of the bond prospectuses. Only the portions that are pertinent to the present study will be discussed.

The Massachusetts Port Authority (Massport) operates Boston Logan International Airport. It is a compensatory approach airport. The following excerpts are from the prospectus of a bond issue that was offered in Autumn, 1984. The funds are to be used for improvements to several Massport properties, with a large portion earmarked for the airport, which is Massport's main source of revenues.

In the section "Description of the 1984 Bonds", the terms of tender (sale), interest payment and redemption are described. For this particular issue this section is quite long, as this is an adjustable rate bond with complicated terms. The fact that Massport has chosen this type of financing reveals a great deal about its assumptions (and the financial market's assumptions) regarding the fiscal health and future prospects of the Authority. In describing the interest rate, the prospectus states:

> The annual rate of interest to be borne by the 1984 bonds for each six month period...will be adjusted to the interest rate determined by the Remarketing Agent as the minimum rate that would then be required to remarket the 1984 Bonds at par.[22]

The interest rate is to be paid every six months, as is commonly done, and the process by which this rate is determined is as follows: Massport's Remarketing and Indexing Agent, an investment banking firm, determines an average of then-current yield evaluations, at par, of at least five tax-exempt securities having a remaining term, as nearly as

possible, equal to six months and a comparable rating to the Massport bonds. Using this average as guide, the agent then determines the minimum interest rate that would then be required to remarket the Massport bonds at par (face value).

Bondholders are notified of this rate, and given twenty days to dispose of their bonds, if they wish. This is called Optional Tender, and the procedure for it is also outlined in the prospectus: Massport has executed a Standby-Purchase Agreement with a major bank. If bondholders wish to sell their bonds on or before any Interest Payment Date, they sell them to Massport's Tender Agent. The bonds are then remarketed in the secondary bond market, repurchased by Massport if it chooses to retire them, or purchased by the bank. According to the Standby Agreement the bank has agreed to purchase, at par, any 1984 bonds which are not repurchased or remarketed.

If Massport wishes, it may establish a fixed interest rate, effective on any Interest Payment Date, and continuing until the bonds mature or the entire issue is repurchased. If a fixed interest rate is deemed to be necessary, it will be determined by the Remarketing and Indexing Agent in manner similar to the adjusted interest rates. It will be based upon tax-exempt securities having a remaining term equal to the time remaining until the maturity of the 1984 bonds. Massport will assume at this time that all bondholders wish to tender their 1984 bonds, unless the bondholder notifies the Tender Agent in writing. This arrangement is essentially protection for Massport from interest rates that become too high.

Massport covenants to use "its best efforts" to maintain a standby purchase agreement with the present bank or some other financial institution as long as any of the 1984 bonds are outstanding and no fixed interest rate has been established. The current agreement

with the bank commits Massport to repurchase any 1984 bonds which are purchased by the bank in equal quarterly installments over a period of seven years, from a fund established for this purpose. The bank is also to receive a fee for these services from monies available from the same fund.

Prior to setting a fixed rate, these bonds are subject ot optional redemption by Massport on any Interest Payment Date, at par value. After the setting of a fixed rate, if this were to happen, a schedule is presented detailing when Massport has the option of calling these bonds prior to maturity.

Some discussion of how bond yields are determined is in order, here. The yield-to-maturity of a bond is the average yearly rate of return on the investment. Because bonds do not necessarily sell at their par value, and because the stream of income is discounted over time to calculate the present value, the actual coupon rate of a fixed interest bond is not necessarily the yield rate. The yield rate takes the other factors into account, as well.

Of equal importance is that investors generally require a higher yield for a longer-term bond. They exact a premium for risk (no one knows what will happen to the issuer or the economy before the bonds mature, and uncertainty increases as the years to maturity increase) and a premium for sacrificing liquidity (by tying up money for long periods).

Because Massport will be indexing its interest rates based upon securities scheduled to mature in six months, it will, in effect, be paying lower, short-term rates. Securities due to mature in six months will be selling at, or close to, par value. This is for several reasons. First, the uncertainty regarding default is almost nonexistent, and there is little restriction on liquidity, meaning no

liquidity premium is required. Further, no bondholder will sell for below par knowing that in six months the bond will be redeemable at par.

The Standby Agreement with the bank further insures that the price of the bond will never fall below par on the market, because if it did, no one would sell at that price. Bondholders could simply tender their bonds to the bank for full par value. Massport, in effect, has a guarantee from a major bank for its bonds, and this enables it to pay lower interest rates. It is easy to see why a bank's guarantee has more value than that of a group of airlines using the airport. The fact that the bank is willing to enter into such an agreement is a further signal to prospective investors of Massport's financial health.

The bond prospectus goes on to describe the security for the 1984 bonds as "a pledge of the Authority's Revenues, which include all tolls, rates, fees, rental and other charges from its Projects and certain investment income and other revenues." In a description of the airport and its potential earning power, the following statements appear:

> The Authority estimates that greater than 90% of total passengers have their origin-destination point at the Airport. This is in contrast many other major airports which are used by airlines as connecting hubs for passengers enroute from another point of origin to another point of destination. As a result, overall airport traffic is not vulnerable to significant fluctuations in connecting traffic resulting from route restructuring or other factors affecting particular airlines....Growth rates in the markets served from the Airport have varied since Airline Deregulation in 1978, but the basic travel patterns have changed little....
>
> Since Airline Deregulation in 1978, total passenger traffic at the Airport has increased by 45.6%....Under deregulation growth in passenger traffic at the Airport has consistently exceeded that for the nation as a whole....The

> Authority does not expect that the failure of any one airline serving the Airport would have a significant effect on Airport operations and finances.

The prospectus goes on to describe sources of airport revenue, including a cargo and mixed-commercial-use complex currently being developed on airport property. In a discussion of revenues from landing fees, automobile parking, and terminal rentals it is pointed out that landing fees, utility and terminal charges are set to recover direct and allocated costs, including administrative and capital cost, and that:

> Unlike many airport operators, the Authority is not constrained by contractual arrangements with the air carriers governing incurrence of landing field costs and the recovery of such costs in the landing fee.

On the other hand, steady increases in airport net revenues since 1980 are attributed to growth in parking, rental car and other concessions. Logan, then, far from totally dependent upon the airlines for its debt retirement funds and, therefore, for its capital expenditures.

The City of Atlanta owns and operates Hartsfield-Atlanta International Airport, which is one of the busiest airports in the world. The CBO survey describes it as a residual-cost approach airport, with the exception that terminal concession revenues are shared by city and airlines.[23] The prospectus considered here is for refunding bonds issued prior to 1982. The object is to restructure the debt to provide long-term financing, as well as to remove restrictive

covenants found in the prior bond agreements, "thereby facilitating future airport improvement and expansion."[24]

The prospectus begins with a general overview of the bond issue and its terms. This introduction states that the bonds are secured by "a pledge of and lien upon Net Airport Revenues." These particular bonds are subordinate to some of the Airport's other debt, meaning that the other debt has a prior claim upon repayment, should monies be insufficient to cover both.

The introduction goes on to say:

> The major portion of Airport Revenues are derived by the city from agreements entered into with Air Carriers utilizing the Airport. The ability of such Air Carriers, individually and collectively, to make payments required under such agreements may be affected by certain factors relating to the air transport industry.

The description of the 1982 Bonds, in contrast to the several pages required to describe Massport's 1984 Bonds, fills only one-and-one-half pages. This is a very straightforward and standard offering. It consists of some serial bonds and some term bonds, enabling the airport to repay the debt gradually over fifteen years and granting the advantages of long-term debt in the form of term bonds maturing in twenty and twenty-five years, respectively. The bonds are coupon bonds, and their interest rate is fixed.

The prospectus states that airport revenues are derived primarily from:

(1) passenger terminal leases,

(2) landing fees,

(3) airport concessions,

(4) rental of office and warehouse space to the principal concessionaire at the airport,

(5) leases with four airlines for space for flight support activities such as food preparation, cargo, etc.,

(6) separate agreements for use of the international arrivals space (the Federal Inspection Services (FIS) Facility),

(7) cargo and maintenance area leases,

(8) "other agreements" relating to commercial activities on the airport.

It goes on to point out that:

> The agreement of the City to adjust [its rates] is subject to the condition that, because the City has entered into certain long-term contracts, the City may be limited or prevented from making [such changes] under such contracts during their respective terms.

In fact, debt service requirements are part of the formula used to determine rental rates. These costs are allocated to the various users and multiplied by a "cost factor" of 1.20--the level of debt service coverage covenanted for in the bond prospectus. The factor of 1.20 is specified in the lease agreements, and if total airport revenues should prove to be inadequate to cover debt service requirements, the airport has no recourse for increasing the cost factor. Since lease terms all began in September, 1980, when the new facility at Hartsfield was completed, and all continue for thirty years, Atlanta has little flexibility to respond to unforeseen occurrences and cover itself, financially.

Despite expectations for passenger growth, Atlanta saw a decline of both passengers and aircraft operations in 1979 and 1980, respectively. It is also significant that two airlines, Delta and Eastern, together accounted for 91% of passenger enplanements in 1981.

The City Department of Aviation estimated that the airport's passenger traffic in 1982 consisted of 65% transfers and only 35% originating or terminating passengers.

The prospectus publishes highly detailed information on Atlanta's air traffic by carrier. The implication is that the airport is dependent upon specific carriers maintaining their hubs in Atlanta. It is stated that the financial information reported in the prospectus is based upon the assumption that the air carriers, "particularly Delta and Eastern," will continue to use Hartsfield as a major hub.

The bond prospectuses of the two airports paint two very different pictures. Boston has an airport which is supported by a diverse financial base, which draws traffic on the merits of the region it is in, and which is not dominated by any airline. It has been able to create relatively low-cost financing for itself, based upon its sound financial condition, and with the support of the financial community (whose motives, it can be assumed, are not altruistic).

Atlanta Airport, on the other hand, is a brand new, expensive facility, highly dependent upon two airlines--one with a history of serious fiscal problems--for its revenues and its traffic. Its bond rating, as mentioned earlier, has suffered as a result of this, and its cost of capital is likely to be higher.

Another marked difference between Boston and Atlanta is that Atlanta has definite capital expansion plans for its terminals and airfield (a new concourse is part of the master plan and a fourth runway was recently completed). Boston does not have such plans because of stringent social, political, and environmental constraints on expansion. Massport's one extensive capital improvement plan for the airport, the commercial use area called Logan South, may represent a sounder move in terms of fiscal health, however. Atlanta's airport,

in contrast, is firmly committed to investment in aviation. In order to further solidify its attractiveness to airlines, given its high percentage of transfer passengers, this may be a necessary stance. It necessarily narrows Hartsfield's financial base, however, and strengthens its dependence on the goodwill and financial health of the airlines. Examination of these two prospectuses seems to bear out the observations and insights of the CBO study that the financially stronger airports are compensatory approach airports, and that a strong local economy and diversity of revenue sources have become more important for airports than long-term commitments from airlines.

There are, of necessity, financial ties and interdependencies between airports and airlines because neither could exist without the other. As it becomes necessary for these ties to loosen somewhat, there must be other sources of financing available to airports. These are accessible from the private sector for financially sound airports. Less fiscally healthy airports, however, do not have the same access to private funds. For them, a vicious cycle is created that makes them more dependent upon airlines (and the Federal government) and less able to create an independent base that would give them greater access to private funds.

It is difficult to predict what the end of the story will be. Deregulation may be the deciding factor, in the end, because the network fluctuations which have resulted from it have yet to stabilize. At present, then, the key for airports seems to be to maintain as much financial flexibility as possible.

# CHAPTER THREE: AIRPORT LEASES AND USE AGREEMENTS

In the previous chapters, the lease agreement was examined as an instrument for formalizing the financial relationship between an airport and the airlines serving it. The lease, of course, serves other purposes in the airline-airport relationship. Primarily, along with financial obligations, the lease governs the use of space at the airport, and the use of space has become an issue with important implications which will be examined in this chapter.

The problems which are beginning to surface in regard to space allocation arise out of the fact that efficiency had not been an important criterion in the past. An example of how this situation is beginning to draw more attention can be found in an office memorandum of March, 1979, by a member of the San Francisco Airports Commission, which stated, "Space is a limited resource the allocation of which has not been based on any rational formula established by the airport operator." The author went on to consider five alternatives as solutions to the problem:[1]

(1) The airport operator could continue the practice of constructing space according to airline requests. The problems with this approach are that it is expensive and would cause proliferation of terminal facilities. On the other hand, the airlines are in the best position to gauge their own needs, and this approach might be acceptable if the airlines paid their own costs. If airline needs are in conflict with the needs of the local community, another alternative must be found.

(2) The airport operator could develop total space needs on a formula basis and allocate it on percentage of use

basis. This approach would provide, theoretically, the most efficient use and fairest distribution of space, but the formula would be complex and require the airport operator to be extensively familiar with the airlines' operational requirements.

(3) Airlines could voluntarily develop joint usage plans for boarding and baggage areas and ticket counters. This approach may not provide efficiency since it depends upon the airlines' willingness to cooperate, an occurance which has not always been enhanced by the increased competition since deregulation. Also, airlines which start out with more space are in a controlling position.

(4) The airport could increase the cost of terminal space to the point where the airlines would be encouraged to seek sharing arrangements. Some airlines, however, could afford to cover such costs for a time and wait for the less financially sound carriers to be priced out of the market. The airport would then be accomplice to undercutting competitive, but poor, new carriers.

(5) The airport could offer space on an open bid basis. This proposal suffers from the same drawbacks as (4), above. In addition, it would be difficult and costly to administer.

Space allocation and usage, as mentioned before, is delineated in an airport's lease agreements, and it is also common, although not universal, to find airfield space governed by a use agreement between airport and airlines. A use agreement provides for the use of property by non-owners of that property. A lease is an agreement for the

exclusive use of property for a stated time period. Some airports use both kinds of agreement, with the use agreement covering the use of the airfield, and the lease assigning terminal, gate, and apron space. A lease will almost certainly provide for unrestricted access to the leased premises, so that lack of a formal use agreement has no material effect. Separate leases will also cover rental of airport land for maintenance, ground service, and cargo facilities, etc. At some airports leases are negotiated with tenant airlines as a whole and are standard throughout the airport. At others, leases are negotiated on a tenant-by-tenant basis, and some airports, including one covered by this study, have placed several renting airlines on a month-to-month, tenant-at-will basis with no agreement at all.

While the need for leases has usually been taken for granted, the question of whether an airport should, in fact, negotiate and sign a lease is relevant in today's aviation environment. An airport authority needs to consider whether terminal space is scarce at the airport, and whether the ability exists to expand in a cost-effective manner. As discussed in Chapter Two, the need for a secure flow of rental income to amortize debt is another important factor. The third point to consider is the nature of the working relationship with the carriers serving the airport, and whether it is desirable to guarantee them the space they require. In addition, the airport must consider whether it has the ability to negotiate for strong provisions in areas where it recognizes a need for more effective airport management.[2]

A further basic question regarding lease agreements is whether or not there should be a standard, uniform lease for all carriers serving the airport. Some of the issues in having uniform agreements with every carrier are:

(1) Uniform long-term leases limit the flexibility of carriers, and some may find this undesirable. Long-term leases can also limit the ability of a new entrant to find terminal space at an airport. Both of these problems, however, can be circumvented by giving carriers the ability to sublet terminal space. (Subleases raise other questions, however, which will be considered separately.)

(2) Different carriers have different operating requirements and planning horizens. Uniform leases may prevent a carrier from offering optimal service at a particular airport.

(3) From the airport management's point of view, uniform leases are easier to administer, but may be harder to negotiate, because of the need to come to agreement with several carriers over one document. Leases which vary from carrier to carrier, however, may give rise to problems if one carrier is granted better terms than those given to other carriers.

(4) When the airport is dependent upon its leases for repayment of outstanding revenue bonds, the airport operator has less leeway to negotiate on individual terms with a carrier. Uniform leases with uniform rental rates, calculated to cover operating expenses and debt requirements, can offer more assurance that debt-repayment requirements will be met.

Although this study will focus primarily on seven particular aspects of lease and use agreements, some background on the range of clauses and provisions typically found in these documents will be useful. In 1979, a survey of twenty-seven airport - air carrier leases was performed by the Federal Aviation Administration (F. A. A.) Office

of Aviation Policy. The report on the survey described the common features of these leases, and the following is a summary of those descriptions:[3]

(1) Length of Agreement - The average term of the twenty-seven leases examined was twenty-five years, with most of them providing for escalation of fees during the term of agreement.

(2) Exclusive-Use Areas - Several of the documents defined exclusive areas of use including ticketing, baggage, holding lounge, and ramp areas.

(3) Common Areas - Some agreements defined common areas, e.g. walkways, lobbies, and access roads, and explicitly give carriers rights to use these areas in common with others.

(4) Preferential-Use Areas - This phrase was applied to space which might be used by a second carrier at times that the leasing carrier was not using it. Such arrangements usually applied to gates, ramps, and skyways. Only seven of the surveyed leases contained this provision.

(5) Severability - If a court declared a section of an agreement to be invalid, this clause provided for excising the invalid section while declaring the intent that the rest of the agreement remain in force.

(6) Quiet Enjoyment - The lessor guaranteed that it would not interfere unreasonably with user's enjoyment of the property.

(7) Unrestricted Access - The airport guaranteed to the carrier that it, its employees, and its customers would

always have a reasonable means of access to the carrier's leased areas, although not necessarily by the same route.

(8) Provision for Future Construction - In anticipation of airport expansion or reconstruction, the airports surveyed made provisions for changes in three different ways: (i) the lease might describe an already-planned building program, or (ii) it detailed how the parties would deal with future construction, or (iii) it provided for changes in fees as new facilities came into use. This type of clause appeared in ten of the leases.

(9) Equal Fees - The airport agreed not to charge the carrier more for a service or area than it charged other users. Only four out of the twenty-seven made this provision.

(10) Equal Privileges - As well as equal fees, the airport guaranteed it would not provide more generous terms to any other airline. Twelve of the twenty-seven made this provision, and, with one exception, they were not the same ones who had equal-fees clauses.

(11) Subordination - The agreement was subordinated to laws of the state or Federal Government.

(12) No Waiver of Default - If one party defaulted on its obligations according to the agreement, the default was not considered waived by the other party simply because the second party did not take immediate action.

(13) Airport Fees - The agreement specified the nature and extent of airport user fees. There are many kinds of

TABLE 3 - 1: FAA SURVEY OF AIRLINE-AIRPORT LEASES

Agreement components:

1. A. Lease; B. Use Agreement; C. Both Lease and Use Agreement
2. Length of Agreement in Years
3. Exclusive Use Areas
4. Common Areas
5. Preferential Use Areas
6. Severability
7. Quiet Enjoyment
8. Unrestricted Access
9. Provision for Future Construction
10. Equal Fees
11. Equal Privileges
12. Subordination
13. No Waiver of Default
14. A. Fees Based on Aircraft Landing Weight; B. Rent Based on Square Footage; C. Fees Based on Number of Enplaned Passengers; D. Fees Tied to Bond Financing; E. Minimum Fee
15. Carrier Review of Budget
16. Arbitration of Disputes
17. Prohibition on Use of Adjacent Airports
18. Force Majeur Including Government Requirements
19. Forbids Denial of Civil Rights
20. Forbids Unreasonable Withholding of Consent
21. Writing Constitutes Entire Agreement
22. Assignment/Sublease Clause

| Airport Agreement | 1A | 1B | 1C | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14A | 14B | 14C | 14D | 14E | 15 | 16 | 17 | 18 | 19 | 20 | 21 | 22 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1. JFK Unit Terminal | X | | | [illegible] | X | | | | X | X | X | | | X | X | | X | | | | | | | X | | | X | X |
| 2. JFK Wing Building | X | X | | [illegible] | X | X | | | X | X | X | | X | | X | | X | X | | | | | | X | X | | X | X |
| 3. Atlanta - 1960's | | X | | [illegible] | | X | | | | X | | X | | X | X | X | X | | X | X | | | | | | | | X |
| 4. Atlanta - United | | | X | [illegible] | X | | X | X | X | | X | | X | X | X | | X | | | | | | | X | X | X | | X |
| 5. Atlanta - CPTC | X | | | [illegible] | X | | X | X | X | | X | | X | X | X | | X | | | | | | | X | X | X | | X |
| 6. Atlanta - New Terminal | X | | | [illegible] | | | | | | X | X | X | | X | X | | X | | | | | | | X | | | X | X |
| 7. Nashville | X | | | [illegible] | X | X | | X | X | X | | | X | X | X | X | X | X | X | X | X | X | | | X | X | X | X |
| 8. Detroit | X | | | [illegible] | | X | | | X | | | | X | X | X | X | X | X | X | | X | X | | | X | X | | X |
| 9. New York - LaGuardia | X | | | [illegible] | X | | X | | X | | | | | | X | X | X | | | | | | | | | | | X |
| 10. Boston - Logan | X | | | [illegible] | X | | X | X | X | | X | | | | | | X | | | | | | | X | X | | | X |
| 11. FAA - TWA | X | | | [illegible] | X | | | | | | | | | | | | X | | | | | | | | | X | | |
| 12. FAA - 1975 | X | | | [illegible] | X | | | | | | | | | | | | X | | | | | | | | | X | | |
| 13. FAA - #5100 | | X | | [illegible] | | X | X | | X | | | | X | | X | | X | X | | | | X | | | X | | | X |
| 14. FAA - #5182 | X | | | [illegible] | X | | | | | | | | | | | | X | | | | | | | | | | | |
| 15. FAA - Exhibit G | | X | | | | | | | | | | | | | | X | X | | | | | | | | | | | |
| 16. FAA - VIASA Airlines | | X | | [illegible] | | | | | X | | | | X | | X | X | X | X | | | | | | | | X | | X |
| 17. Dallas-Fort Worth (DFW) | | X | | [illegible] | X | X | | X | X | X | X | X | | | X | X | X | X | X | X | X | | | X | X | X | X | X |
| 18. DFW - Delta | | X | | [illegible] | X | | | | | X | X | | | X | | X | X | | X | X | | | | X | | X | | X |
| 19. Dade County | | X | | [illegible] | | | | | | X | | | | | | X | X | | | | | | | | | | | |
| 20. Dade County (Miami) | X | | | [illegible] | | X | | | | | | | | | | X | X | | X | | X | | | | | | | |
| 21. Houston | | | X | [illegible] | X | X | X | X | X | X | | | X | | X | X | X | X | | | X | | | X | X | X | X | X |
| 22. El Paso International | X | | | [illegible] | X | X | | X | X | | X | | | | X | X | X | | | | | X | | X | | | | X |
| 23. Orlando | | | X | [illegible] | X | X | | X | | | | X | X | X | | X | X | X | | | | | X | | | | | |
| 24. Baltimore | | | X | [illegible] | X | | X | X | X | | | | | X | | | X | | | | | | | | X | | X | X |
| 25. Cincinnati | | | X | [illegible] | X | | | X | X | X | X | | X | | X | | X | | | X | | | | | | | | X |
| 26. Chicago - O'Hare (Lease)* | X | | | [illegible] | X | X | | X | X | X | | | X | | X | | X | | | X | | | | | | X | | X |
| 27. Chicago - O'Hare (Use Agreement)* | | X | | [illegible] | | X | | X | X | | | | X | | X | X | X | | X | X | | | | | | X | | X |
| 29. Newport News - Patrick Henry International* | | | | | | X | | X | | | | | | | | X | X | X | | | | | | | | | | |
| TOTAL ALL AGREEMENTS | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] | [illegible] |

Source: Federal Aviation Administration

fee arrangements, but there were some common features in the leases examined:

(a) Fees based on landed weight: the maximum landing or take-off weight of each aircraft for each landing is usually the basis for what have come to be known as landing fees.

(b) Rent based on square footage: this is a common scale of charges for exclusive use areas, and also for common use areas, although it does not necessarily represent the use a carrier makes of the latter. All twenty-seven agreements contained provisions for this type of charge.

(c) Fee based on number of enplaned passengers: nine of the documents carried provisions for such a charge, which is useful in assessing costs of security, passenger waiting areas, etc.

(d) Fees tied to bond financing: seven of the leases had a calculation element which linked fees to bond financing requirements. For example, the airport required a surcharge in years when revenues were low or maintained a surplus fund from good years.

(e) Minimum fee: usually a minimum landing fee. Seven agreements carried a minimum fee provision.

(14) Majority-In-Interest (MII) - The carriers were given the right to review the airport budget, and in some agreements a "majority-in-interest" could veto items in the budget. A majority-in-interest was usually defined

as fifty-one percent of the carriers at the airport and enough carriers to constitute fifty to seventy-five percent of the total landed weight of the preceding year. Five of the surveyed leases had this clause. (Provisions of this sort will be examined in greater detail, later in this chapter).

(15) Arbitration of Disputes - Disputes could be submitted to binding arbitration, with both sides, usually, splitting the cost.

(16) Prohibition on Use of Adjacent Airports - Some agreements prohibited the carrier from using any other airport within twenty-five to fifty miles of the airport.

(17) Civil Rights Clauses - More recent agreements carried a requirement that the airline not discriminate.

(18) Forbids Unreasonable Withholding of Consent - The airport agrees not to withhold consent without reason, when that consent was required for a proposed action of the carrier.

(19) Writing Constitutes Entire Agreement - Outside discussions, letters, etc., are not a part of the legal agreement. The lease document alone is considered to express the intent of the parties at the time of its signing.

(20) Assignment/Sublease Clause - An assignment is the transfer of a party's complete interest in land, both as to extent and duration. A sublease is a transfer of less than a complete interest in the land, either as to extent or duration. The legal significance is that a sublessor remains liable for the property, but if

interest is assigned, there is no further obligation. This clause provided that a carrier must receive the airport's permission to sublease, while the airport agreed not to unreasonably deny permission. The carrier did not need permission if the party receiving the carrier's interest was its parent company or a company into which it was merging.

(21) Right of First Refusal - Several agreements granted carriers right of first refusal regarding space that became available, before giving new entrants access to it.

In addition most agreements provided for insuring leased areas, for maintenance and utilities, and defined what concessions a carrier could operate. Some features of interest that were unique to one agreement included:

(1) In contrast to most leases, one specified that agreements made pursuant to it would not supercede existing agreements.

(2) Another provided for the carrier to have joint occupancy if expected new terminal construction were to be deferred.

(3) One allowed carriers to cease payments if they lost their operating authority, but required of them a lump-sum payment of three times their annual fee if outstanding bonds existed at that time.

(4) One F. A. A. agreement made explicit provisions for space reallocation to accommodate new entrants.

(5) A LaGuardia agreement limited stage lengths of flights to it until 1964 and placed limits on aircraft types

which could use the facility--this was, presumably, typical of all LaGuardia leases.

(6) One airport allowed carriers to sublet parts of its areas if (i) it no longer needed them, and (ii) the airport refused to take back possession.

(7) J. F. Kennedy Airport provided for some new construction by specifying that much of it be done by the airlines, after which it became property of the airport.

(8) Another agreement provided for termination if the parties could not agree on a fee schedule or could not find a basis for cooperation in expansion plans.

(9) An example of providing for bond-repayment security was that a carrier not be allowed to terminate for any reason until airport bonds had been retired. After that, termination was allowed for any reason, provided notice was given.

(10) O'Hare's use agreement required airlines to agree to actually use the airport for the whole term of agreement, rather than just pay fees.

This thesis will concentrate upon seven aspects of airport-airline agreements, in addition to the issues of financing and rate-setting which have already been mentioned. Each of them exerts a significant influence upon the distribution of power and management responsibility at an airport. They are:

(1) The existence and purpose of the use agreement;

(2) Majority-in-interest clauses;

(3) The length of the lease-term;

(4) Provisions for carriers who wish to become new entrants into the market;

(5) Provisions for subleasing terminal and apron space;

(6) Provisions for levels of gate utilization, and for airport recovery of control over underutilized gates;

(7) Termination clauses.

## Use Agreements

Use agreements do not exist at every airport, and, in terms of their function of granting access to and use of the airfield, they are not really necessary. The lease implies these rights in most cases, and, should the carrier not lease directly from the airport, the Federal Government has some say in such matters, as well.

The airlines appear to be the ones who favor use agreements, because they have been the vehicle which formalized carrier influence over airfield operations and, especially, airfield expansion. The negotiating process which is usually involved in signing any agreement gives carriers a voice in the level and structure of the landing fee, and the operations on the airside. Airports which do not have use agreements (or include clauses of this type in the lease) can simply present the desired landing fee to the airlines and oversee the airfield through Airport Rules and Regulations. Some airports have chosen not to have use agreements for just this reason.[4]

As airfield capacity becomes more and more constricted at some airports, the existence of a use agreement can hinder the airport authority in attempting to deal with the problem, especially if these agreements run for a long term. Alterations to the landing fee, e.g. peak-hour surcharges or raised minimum landing fees, may be difficult or impossible to institute. Further, if airports begin to institute

slot allocation systems, other problems will surface. Airports often grant more favorable terms to use agreement signatory carriers than those given to "non-sigs", and use agreements guarantee certain rights of airfield usage to signatory carriers. Any attempt at slot allocation could be faced with issues of the rights and privileges of signatory carriers over non-signatory carriers and new entrants. The airport sponsor might thus be prohibited from forming an equitable and efficient plan for allocation.

## Majority-In-Interest Clauses

The question exists as to what extent airlines should have a voice in an airport's capital investments: both in on-airport development and off-airport expenditures on rectification of airport-generated environmental problems. This question is answered at each individual airport by the existence or non-existence of MII clauses in the lease agreements. The extent to which these clauses give the airlines influence over airport policy and operational decisions varies, and these variations can reveal much about the nature of the airline-airport working relationship.

The question that the airport must consider is that of retaining its discretionary power to accomplish projects which the carriers see as unrelated to, or even detrimental to, their operations at the airport. In coming years, airport management may also find that it needs to concern itself with the antitrust implications of MII clauses, as well as MII influence over airport access decisions.[5] Airports with MII clauses may find themselves unable to make capital expenditures to provide space for new entrants, because the incumbent carriers may veto the action in an effort to keep out new competition.

In the 1979 F. A. A. survey, it was noted that because a number of agreements made explicit provisions for payment of bonded indebtedness from fees paid by carriers, there was a natural concern that airports would be tempted to build indiscriminately at the carriers' expense. Therefore, agreements often provide for carrier review of the airport budget, often in the form of an MII clause. In some cases, the carriers had the ability to prohibit the airport from making expenditures.

Some examples of such provisions are:[6]

(1) A carrier can review items in the current budget, which usually include daily operating expenses. The carriers meet with airport management to discuss the budget before it goes into effect, but carriers cannot present any expenditure from taking place.

(2) A carrier can review items in the capital budget. The capital budget includes items used for longer than a fiscal year, and, again, the carriers can meet with airport authorities and discuss the budget, but not veto.

(3) An MII can review items in the current budget, but cannot veto any item.

(4) An MII can review items in the capital budget without the right to veto.

(5) An MII can veto items in the current budget. Such clauses are usually limited so that carriers cannot prevent the airport from expanding facilities to include new entrants nor prevent the airport from complying with any government regulation.

(6) An MII can veto items in the capital budget. Usually only construction above some specified threshhold amount

can be vetoed. The limitations written into clauses as in (5), above, would also apply here.

(7) A carrier can refuse to pay for capital improvements if it objects to the construction at the time it is proposed.

Many of the agreements surveyed in 1979 included more than one of the above provisions. Particularly, those providing for individual carrier review and MII review were often found in the same leases.

Length of the Lease Term

Long-term leases--of twenty-five to thirty years-- were once the norm in American aviation. The trend toward more airport control and flexibility has caused this practice to be reappraised, and one of the questions commonly being raised regarding airport leases is what the appropriate length of term should be. Some considerations for airport administrators in deciding this issue are:

(a) whether there is a need for flexibility to reassign terminal space and whether such space is a scarce resource;

(b) the length of time required to retire outstanding revenue bonds issued to finance the facility, and the level of debt involved;

(c) availability of unassigned space in the terminal under the control of the airport sponsor;

(d) the degree to which the facilities are being built to individual airlines' specifications.[7]

Some airlines also prefer short term leases because they can exit an unprofitable market with more ease. They, too, are finding that they sometimes need flexibility.

Chapter Two dealt with the financial advantages and disadvantages to the airport of short- and long-term leases. The 1979 F. A. A. survey prophetically reached similar conclusions:

> In time, it seems likely that the larger, more popular airports will dispense with long-term agreements without losing any real advantages. Since the airport will always have business from its local market, the long-term leases really provide no more stability than is already there.[8]

Accommodations for New Entrants and Subleasing

An airport's provisions for carriers which are new entrants to a market have come under increased scrutiny since deregulation. The Federal Government is concerned that airport leasing practices may act to restrict the freedom of competition which the Airline Deregulation Act was written to create and encourage.

In a letter to the Secretary of Transportation in late 1978, Marvin Cohen, who was then Chairman of the C. A. B., pointed out:

> At many major airports the methods employed to allocate landing and takeoff opportunities and other airport facilites among air carriers may act as barriers to entry which discourage carriers from offering new or expanded service at those airports.

He cited the example of two airlines, which were authorized to intitiate service to and from Midway Airport in Chicago and which found that all gates and counter space were under contract to existing carriers, "despite the fact that they had conducted almost no operations at Midway for ten years." (emphasis in text).[9]

The 1979 F. A. A. survey was originally performed partly to investigate the lease agreement as an effective barrier to entry of new carriers, and it expressed similar concerns. The study observed that many airports used long-term agreements with their airlines, and that, while they were mutually beneficial to airport and resident carriers in providing stability, they made little provision for new entrants to the airport. It went on to say, however, that new entrants had had little trouble finding access in actual practice. The reasons given were that agreements could be revised by supplemental agreements, and that carriers have been inclined to cooperate with one another by subleasing. The value of an airport to a carrier often is enhanced by having more carriers, and, also, airlines know that cooperation to one's advantage in one market can be reciprocated to the other's advantage in another market.[10]

If airport capacity becomes more constrained, however, and competition for market shares becomes fierce, subleases are not going to be an adequate mechanism for accommodating new entrants. The motivation to keep a competitive carrier out may overwhelm any of the advantages of a subleasing arrangement.

Sublease clauses often grant the airport the right to approve an arrangement made between two carriers, but they have rarely given the airport the right to actually require such an arrangement. An illustration of the type of provisions which will become necessary at some airports can be found in the carrier agreements at Washington National Airport, perhaps the ultimate current example of a capacity-constrained airport. The following provisions are from the Metropolitan Washington Airports (M. W. A.) Use Agreement:

If a scheduled carrier wishes to initiate service at a M. W. A. airport, the following steps will be taken in order to secure terminal space for the new entrant:

(1) If the Government has space available which will meet the carrier's requirements, it will lease it directly to the carrier.

(2) The requesting carrier and the Government will conscientiously attempt to make voluntary arrangements witheach of the other Authorized Carriers (those which have signed the Use Agreement) serving the airport to either handle the operations of or share their leased facilities with the requesting carrier.

(3) If no such agreements can be reached, and the Government has, with no success, given sixty days to all Authorized Carriers to attempt to reach an agreement with the requesting carrier, the Government then has the right to give an Authorized Carrier sixty days further notice to accommodate the requesting carrier.[11]

Recovery of Control Over Gates

Lease agreements have, traditionally, given the major part of control over exclusively-leased areas to the airline. More recently, however, some airport administrators have felt the necessity to recover some of this control, especially over gate areas, in order to make more efficient use of limited space. Airlines are naturally reluctant to have an already difficult scheduling process further complicated by having to share or give up gate space at some airports. Issues such as these have become points of contention in some lease negotiations and are indicative of a need to examine the whole lease/use agreement in a different light.

From the airport's point of view, the power to regain control of underutilized gates and make maximum use of existing space would grant the airport the ability to meet demands of new entrants quickly and to accommodate growth of existing carriers. Officials at airports which have control over some of their gates have reported a higher utilization rate at gates they control than at carrier-controlled gates.[12] This gives the airport the ability to manage its facilities efficiently and meet the needs of the traveling public. Many airport operators have come to feel that the needs of the carriers come second to these priorities.

Gate-sharing is more commonly practiced in Europe than in the United States. There, technically, an aircraft can be assigned to any suitable available gate, however, over time a pattern emerges where carriers are usually assigned certain gates in proximity to one another. Carriers are not granted exclusive use of these gates, which can be assigned on a first-come-first-served basis.[13]

Methods for effective control of the assignment of gates which are either suggested or currently in practice in this country are:

(1) The airport retains complete control over a certain portion of gates and grants no exclusive or preferential rights to this space.

(2) The airport requires sharing of gate-space by lessee airlines under certain prescribed conditions, or it requires that exclusively-leased space be converted to jointly-leased space.

(3) The airport is permitted to reassign exclusive or preferential space under certain conditions, e.g. a required level of gate utilization is not met by the lessee airline.

(4) Exclusive gate assignments are completely avoided, and space is assigned by airport management on a preferential-use basis or a common-use basis.[14]

For example, the M.W.A. Use Agreement gives the airport control over the assignment and use of gates. At Dulles Airport, gates are initially assigned to Authorized Carriers and may be reassigned by M.W.A. at any time. At National Airport, positions were, formerly, preferentially assigned to Authorized Carriers for the term of the Agreement, but carriers were obliged to make their gates available for use by other carriers if requested to by M.W.A. As of January 1, 1985, no carrier has preferential rights to any parking position at National.[15]

At Mueller Municipal Airport in Austin, Texas there are also no exclusively-leased gates, and incumbent airlines have been given "preferential nonexclusive" use of gates instead. The carrier leasing a gate has preference over others to operate its flights, but is not allowed to leave an aircraft at a gate for a prolonged period of time. The agreements also include a formula that pro-rates the cost of the gate among its users.[16]

Gate-sharing requirements and gate-recovery "use-it-or-lose-it" lease clauses are not popular with airlines. This is understandable as controlling gate positions is important to undisrupted airline operations at an airport. Some of the issues raised by sharing of gates, for carriers and airports alike, are:

(1) Passengers may be seriously inconvenienced if the gate from which they depart is located far from the carrier's ticket counters and baggage check-in facilities. For the airport, this may mean devising a new system (and the necessary facilities), allowing these activities to take place at

gates. This, in turn, may mean slowing down movement at the entrance of gate holding areas, and could lead to more congested concourses.

(2) Airlines have traditionally decorated their gate areas as they wished, with airline advertising a part of such "tenant-finishes". Unless the airport is willing to refinish gate areas, passengers may board one carrier's aircraft in the presence of another's advertising. There are, thus, competitive implications to tenant-finishes. Also, the airlines have invested their own money in tenant-finishes and will not, in most cases, have amortized this investment.

(3) Some airlines at some airports lease an entire terminal building and have either provided or guaranteed the financing for construction of that building. In such a case, a carrier might understandably feel entitled to total control over its gates in the building.

(4) Not having complete control over gate usage will limit the scheduling flexibility of a carrier, and this could have repercussions throughout its route network. Further, in a hubbing operation, effective and timely passenger feed depends upon gates being in close proximity to one another. This loss of efficiency can extend to all of a carrier'sairport operations, e.g. aircraft servicing and baggage transfers, at gates which may be distant from one another.

(5) Other competitive issues that may arise are (i) limiting schedule flexibility may limit a carrier's ability to compete through times and frequencies of flight and (ii) competitive flights to the same destination may be assigned to gates

close to one another, a possibility which is not likely to please the carriers.

(6) Different levels of service offered by different airlines extend into the gate area in the form of physical comforts (size of chairs, carpets vs. bare floors), as well as length of queues and levels of crowding. The carriers which provide more luxurious services are likely to object to the possibility of sharing space with a low-cost, low-fare new entrant. The question arises of whether the airport operator should establish a terminal-wide level of service, and schedule gates accordingly.[17]

(7) Other problems which may arise for airport operator in administering shared or preferential-use gates are (i) gates should not be scheduled so that several neighboring gates have peak crowds simultaneously, and (ii) poor on-time performance by a carrier can become an airport-wide issue as gate shifts are required to accommodate late-arriving flights.

## Termination Clauses

Lease termination clauses in pre-deregulation days were of a somewhat pro forma nature. Once an airline received certification to serve a market, everyone assumed (with good reason) that the carrier was in the market to stay--or, at least, for a very long time. Today, however, airlines are born and die, and they come and go, with much more frequency than anyone would have dreamed, just ten years ago. Termination, under such circumstances, has come to mean something--especially to an airport with a great deal of outstanding debt.

Some background on termination clauses can be found in the 1979 F.A.A. survey. It was noted that, short of termination, parties could escape or change the nature of their obligations by subleasing or assigning interests, amending the original agreement as many times as needed, or, if the carrier abandoned and ceased to use all or part of its area, the airport could "reenter and mitigate". This meant the owner might rent the property to another party and apply the proceeds toward the obligations of the original carrier.

If a unilateral termination was necessary, however, the terms by which it could take place were specified. Commonly, clauses stated that the airport might terminate if:

(1) the carrier went bankrupt, into receivership or some similar action;

(2) the carrier lost its authority to fly into the airport (obviously, a pre-deregulation provision);

(3) more generally, if the carrier was prevented from flying into the airport for any reason (temporary problems, e.g. strikes did not activate the clause);

(4) the carrier voluntarily abandoned service to the airport (if the airport had bonds outstanding, the carrier usually agreed to pay a minimum fee to the airport to abandon service);

(5) the carrier failed to perform its obligations, e.g. pay its rent;

(6) in time of war, if the government took all or part of the airport for its use, the airport might terminate the agreement.

For its part, an air carrier might terminate the agreement if:

(1) a court prohibited it from using the airport for a period of time;

(2) the Federal Government prohibited the carrier from using the airport (for leases whose termination clauses predated 1978, the Deregulation Act provided a loophole for unilateral lease termination, at least while the C.A.B. was still granting route authority. The airline could apply to cease service at a particular airport, and once that permission was granted could use the excuse that its right to serve that point had been revoked);

(3) the airport was closed by an unforeseen occurrence for a period of time, unless the occurrence was due to acts by the carrier, itself;

(4) the airport failed to perform its obligations under the agreement;

(5) an obstacle was erected near the airport which prevented the carrier from using the airport for a specified minimum amount of time;

(6) the carrier's contract to carry U.S. mail was terminated;

(7) if the carrier had both a use agreement and a lease agreement with the airport, the cancellation of one allowed the carrier to terminate the other;

(8) any act occurred which deprived the carrier of rights necessary to conduct business (this was a more generalized statement which would include some provisions described above);

(9) because some agreements made provisions for possible new entrant carriers at the airport, the carrier might terminate if, after bargaining in good faith, no agreement could be reached on the reallocation of space.[18]

Many of these termination clauses continue to be written into airline-airport leases. The bankruptcy clause is such an example. Recent events, however, have raised serious doubts as to the effectiveness of bankruptcy termination clauses.

Because airport gate space is so vital to an airline's operation, an agreement granting exclusive use of certain gates has been protected by the bankruptcy courts. It was felt that these gates were essential to any reorganization effort by the ailing carrier. The reorganization petitions, in recent years, by Braniff International and Continental Airlines. are cases in point. Airport proprietors lost control over the gates leased by these carriers (often in spite of provisions in the lease for termination in the event of the carrier's bankruptcy), and, in some cases, the facilities remained empty and unusable when the carrier ceased operations. In other cases, the reorganizing carrier sublet the space, at a profit from which the airport could not benefit.

Because of these experiences, Airport Operator's Council International (A.O.C.I.), has lobbied successfully for an amendment to a new bankruptcy law, enacted in 1984, requiring airlines to give up unused terminal and gate space within a much shorter period of time.[19]

## Conclusion

Roy Williams, the author of the F.A.A. survey, made the observation:

> Agreements between airport and air carriers suffer from two conflicting purposes. On one hand, the parties intend the agreement to be firm and binding. . . . On the other hand, the parties intend the agreement to provide flexibility in the face of changing time and circumstance.[20]

As the leases written even as short a time as ten years ago are filled with clauses which are quickly becoming obsolete, flexibility is beginning to be much more attractive to many airport proprietors--and to some airlines, as well. There is little uniformity, however, among airports. The three case studies which follow deal with three very different airports. While the management of each is aware of the trends and problems others face nationally, their responses to their own situations tend to be very individual. This is illustrative of the fact that, from city to city, the policy positions taken differ according to the immediate needs and problems of the airport, and the priorities of the sponsoring governmental body.

# CHAPTER FOUR: ATLANTA-HARTSFIELD INTERNATIONAL AIRPORT

The William B. Hartsfield Atlanta International Airport had its beginning in 1925 on a vacant speedway nine miles south of the city. By 1928, the city had air routes to Miami and New York, and by the early 1930's had the second largest number of air routes in the country. The first administration building was built in 1932 when American Airlines agreed to advance ten years' worth of rental fees, $35,000, to erect the building. To raise funds for waiting room furniture, Pitcairn Aviation (now Eastern Airlines) donated a plane and pilot to fly sightseers around nearby Stone Mountain. From 1947 to 1961, the airport terminal building was a large war surplus quonset hut.[1]

In 1961, a modern terminal, which could handle 4.5 million passengers per year, was built. By 1967, it was clear that this terminal would soon be inadequate, and plans for today's terminal building were being made. Two years later, the airlines serving Atlanta had withdrawn their commitment to finance this terminal, but by 1975, rapidly climbing passenger loads convinced the airlines that a new, larger terminal was needed, after all. Ground was broken on the midfield terminal, referred to as the Central Passenger Terminal Complex (CPTC), in February, 1977.

The CPTC project was opened to:

(1) relieve congestion caused by increasing numbers of passengers and improve the efficiency of air carrier operations;

(2) provide for future terminal and airfield capacity needs, in anticipation of further passenger growth;

(3) maximize utilization of present and future runways by relocating the terminal and, therefore, changing the pattern of aircraft movements on the airfield

The airport is currently served by twenty-two passenger carriers, and it handled almost 19 million enplaning passengers in 1983, averaging over 50,000 operations per month in that year. Passengers and operations, which had been steadily declining since 1980, were back up to pre-1980 levels in 1983, and one airport official has estimated that 1984 figures will be the highest in the airport's history.

Atlanta has long been a major transfer point in the United States air transport network, and between sixty-five percent and seventy-five percent of its passengers are transfers. As might be expected, this fact has a major influence on the operations and policies of the airport. An equally significant, but somewhat less well-known fact is that Hartsfield, with its affiliated organizations and companies, is the largest private employer in the state of Georgia, responsible for approximately $900 million annually in wages and salaries.

## The Lease and Use Agreements

The terminal leases for the 1961 terminal let to each signatory carrier certain portions of the terminal area. The leases were all substantially the same. Rentals were based upon various charges per square foot and, in certain cases, the costs of some improvements to the terminal area. The portion of rentals related to operating and maintenance costs could be adjusted for each three year period to reflect then-current costs. There were no other provisions in the leases for renegotiating any other rentals charged. The leases were

set to expire on April 30, 1991, a term of thirty years, although each carrier was subsequently given the option of terminating when the CPTCopened, at which time no further passenger service was allowed to operate to or from the existing terminal.[2]

The Old Terminal leases granted exclusive use of certain areas, such as ramp areas and gates, parts of the concourses, and specified portions of the terminal building. In addition, carriers were given the right to use all public space and facilities not exclusively leased to others.

Charges were computed as follows:

(1) Carriers paid rental for gate areas and concourse operational space in monthly amounts, which represented construction and related costs for the terminal area and for tenant finishes in an individual carrier's exclusively leased space. Construction costs were allocated based upon the actual square footage of exclusively leased premises, while the cost of tenant finishes were amortized over twenty years and paid by the individual carriers.

(2) Rentals for exclusively used space in the terminal building were also based upon the overall construction costs for the building. Rates per square foot, however, were not uniform in this case, but were set according to the location of the space leased. In certain cases, carriers paid a fixed sum per square foot, regardless of construction costs. Tenant finishes were sometimes amortized over twenty years and sometimes repaid to the city in a lump sum.

(3) The carriers agreed to pay pro rata shares of fifty percent of annual maintenance and operations costs. Each carrier's share was computed upon the basis of square footage of terminal and concourse space leased to the carrier.

In addition, signatory carriers had right of first refusal on gate space that became available. Carriers could sublease, if the city approved, but not at rentals in excess of those charged the carrier by the city, unless the excess were paid to the city. The city entered into concessions leases and reserved the right to control the sale of food at the airport. The city also agreed not to lease to any other carrier on more favorable terms than those given to signatory carriers, unless those terms were extended to all.

The city could terminate the lease subsequent to any of the following events:

(1) failure of carrier to make rental payments;

(2) carrier's bankruptcy;

(3) carrier's being permanently deprived of the rights and powers necessary to conduct its business;

(4) carrier's abandonment of gate positions and concourse space for a period of thirty days or more, unless that abandonment were due to reasons beyond the carrier's control;

(5) failure of carrier to honor any obligations under the lease.

The carrier had the right of termination if:

(1) the airport Use Agreement were terminated for any legal reason;

(2) breach by the city of any of its covenants under the lease;

(3) continued failure by the city to operate the public aircraft facilities in a reasonable manner;

(4) continued operation of the airport for the accommodation of non-commercial, non-air-carrier traffic to the extent

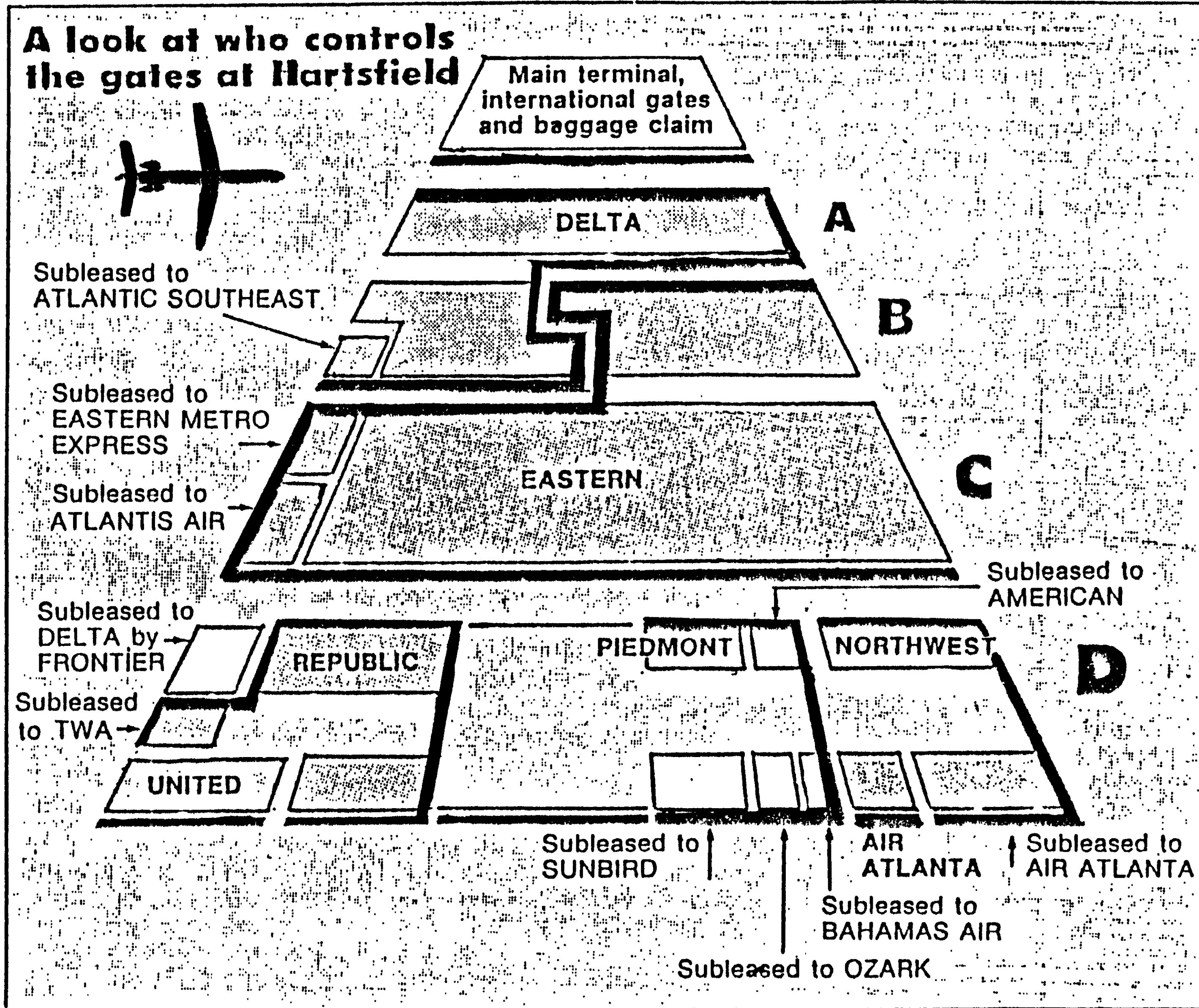
that use of the airport by commercial air carriers is substantially restricted;

(5) carrier is permanently deprived of the rights and powers necessary to conduct its business.[3]

Use Agreements

Use agreements, as separate documents grew out of an older system whereby the city would not sign a use agreement with a carrier who did not lease from the city. When the 1961 terminal was being planned and financing for it was being sought, separate leases for that terminal were written. The lease agreement was thus separated from the use agreement and has remained so, although the two are in effect for the same time periods. The use agreements have been extended to 2010 to match the lease agreements for the CPTC, which also have a thirty year term. Use agreements for carriers who do not lease directly from the city, but sublease from another carrier, will terminate on April 30, 1991, which was the original termination date before the CPTC was built.

Currently, eight of the airlines serving Atlanta have signed leases with the city, and are referred to as the Contracting Airlines. All of the airlines with regular service to the airport have signed use agreements and are designated Signatory Airlines or, in the agreement, itself, the Atlanta Airlines. The eight contracting Airlines are: Delta, Eastern, Piedmont, Republic, Air Atlanta, United, Northwest, and Frontier. Frontier has left the city and sublets its space to Delta. All carriers other than these eight sublease their terminal space from one of these eight.




Source: Atlanta Journal-Constitution, March 31, 1985

Length of Lease Term

The thirty year term of the current CPTC leases began as of the Date of Beneficial Occupancy (DBO) of the new terminal, and the lease specifically states that rentals and charges payable by the lessees, the Contracting Airlines, will amortize the bonds that were issued to finance the project:

> The rentals and charges provided for...shall commence as of the DBO unless the City is required to begin sinking fund payments on the Third Lien Airport Revenue Bonds issued to finance the Project at an earlier time....It is recognized that if monthly Facilities Rental payments commence before the DBO the total Facilities Rental payments over the period prior to the commencement of the lease term and the thirty year lease term itself may result in payments in excess of the amount necessary to amortize the Third Lien Airport Revenue Bonds allocable to Airline Project Costs.... Accordingly, it is agreed that Facilities Rental payments shall be payable only for a total period of thirty years and such Facilities Rental payments, except for the land rental element [for aprons and ramps] shall cease after thirty years notwithstanding the fact that the thirty year lease term will continue for an additional period of time until expiration.

Although long lease terms are partially a carryover from pre-deregulation days, officials from the Aviation Department feel that even now, the bond financing would not be available to the extent needed without long-term leases as collateral; the long term of lease is the only realistic way to amortize the debt so that it is affordable. Also, because only twenty-five to thirty-five percent of Hartsfield's traffic are origin-destination passengers, the facilities at the airport are much more extensive than the local market justifies —or can support.

Airport officials do appreciate the increasing need of modern airports for more flexibility, however. The Airport Properties Manager expressed the opinion, "Under this [aviation] environment we're not that inclined toward long-term agreements in and of themselves. Circumstances don't dictate or justify them....When you don't have that need for long-term financing, short-term agreements are more the norm." He pointed out that many of the subleasing agreements at Hartsfield are for short terms.[4] Experience in Atlanta seems to indicate that the airlines sometimes prefer long-term leases and sometimes not. If a carrier knows it has a long-term commitment to the market (e.g. Delta in Atlanta), long-term leases are preferred. These enable the carriers to do long-term projections and to avoid constant negotiations with the airport.[5]

Amortization of Terminal Costs

Unlike the 1961 terminal agreements, which gave public access to non-exclusively leased space, the CPTC lease designates lessees for almost all of the square footage of the terminal . The agreement states:

> It is acknowledged that the intent of this Agreement is that each airline user of the CPTC shall pay its fair prorata share of the cost of financing, constructing, maintaining and operating the CPTC, which intent shall be effectuated as to the Contracting Airlines throughout this Agreement.

And elsewhere:

> It is understood that the primary purpose of the City in proceeding with the Project is to provide adequate public facilities to accommodate rapidly expanding air traffic at the Airport. After considerable study, City has concluded

TABLE 4 - 1:

## City of Atlanta Department of Aviation Statements of Income (Loss) for the Years Ended December 31, 1983 and 1982

| | 1983 | 1982 |
|---|---|---|
| OPERATING REVENUES: | | |
| Landing fees | $14,161,933 | $14,189,203 |
| Terminal and maintenance buildings and other rentals | 42,931,421 | 41,846,528 |
| Parking, car rental and other concessions | 24,860,536 | 20,287,449 |
| Other | 4,311,236 | 4,590,459 |
| Total operating revenues | 86,265,126 | 80,913,639 |
| OPERATING EXPENSES: | | |
| Salaries and employee benefits | 9,809,971 | 8,248,847 |
| Janitorial and other contractual services | 4,590,400 | 4,121,051 |
| Utilities | 765,359 | 797,728 |
| Materials and supplies | 488,293 | 440,039 |
| Repairs and maintenance | 603,121 | 563,540 |
| General services (Note 2) | 460,796 | 600,504 |
| Provision for alleged noise disturbance and other claims (Note 9) | — | 2,300,000 |
| Other | 2,304,075 | 1,528,329 |
| | 19,022,015 | 18,600,038 |
| Depreciation and amortization | 28,206,724 | 27,204,867 |
| Total operating expenses | 47,228,739 | 45,804,905 |
| OPERATING INCOME | 39,036,387 | 35,108,734 |
| NONOPERATING REVENUES (EXPENSES): | | |
| Interest, primarily on long-term debt, net of amounts capitalized (Notes 1 and 3) | (39,999,425) | (39,153,630) |
| Interest on short-term investments, net of amounts capitalized (Note 1) | 10,313,670 | 17,194,297 |
| Loss on retirement of old terminal facilities (Note 4) | (16,829,912) | — |
| Gain on bonds redeemed prior to maturity (Note 3) | 124,734 | 2,934,984 |
| Other | (24,983) | (24,958) |
| Net nonoperating revenues (expenses) | (46,415,916) | (19,049,307) |
| NET INCOME (LOSS) | $(7,379,529) | $16,059,427 |

Source: City of Atlanta Department of Aviation

> that this purpose can be fulfilled most efficiently and economically by leasing substantial portions of the proposed Project to the Contracting Airlines in order that they and others may provide adequate and efficient air transportation and related services to the public. Accordingly, although the entire Project shall remain public property of the City to be used for public purposes, City intends to lease a substantial portion of the Terminal Building Area to the Contracting Airlines through separate lease agreements substantially the same as this Agreement.

This objective is accomplished in the lease by establishing "Joint Leased Premises" in addition to the exclusively leased space. Joint leased premises are described as being for the airlines' "non-exclusive use in common with other [airlines] as public use space...directly related to the movement of passengers and baggage." (e.g. the concourse walkways). Rentals on the jointly leased premises are allocated among airlines according to six different "Joint Lease Formulas", each of which is applied to a particular portion of the terminal complex. The result is that nearly every square foot of the terminal complex is paying for itself.

This policy has given rise to some controversy, however. When Braniff Airlines, an original CPTC Contracting Airline, went bankrupt a conflict over the jointly leased areas arose between the airlines and the airport. The airport required that the other "joint lessees" assume the share of costs that had been abandoned by Braniff. The airlines disagreed with this interpretation of the lease and the joint lease formulas. The airport appears to have won that argument at this writing.[6]

Rental rates for the CPTC are based upon the cost of the portions of the project which were designated as the airlines' responsibility. These include project costs attributable to the landside terminal buildings (excluding the Federal Inspection Services facility) and the

concourse buildings, the mechanical building, the aircraft parking and ramp area, seventy-five percent of the net cost of two taxiway extensions, and individual tenant finishes, equipment, and systems.

Rentals, in general, are calculated by determining the costs of the various facilities leased and then allocating these costs to each airline according to the percentage of each facility it uses. This allocation is then multiplied by the "Cost Factor", defined below, as quoted from the lease (the resulting figure is divided by the amortization period to determine monthly rental rates):

> The Cost Factor referred to above shall be calculated by dividing the highest aggregate annual principal and interest requirement on all series of Third Lien Airport Revenue Bonds issued to finance the Project...by the aggregate principal amount of Third Lien Airport Revenue Bonds issued to finance the Project and multiplying the result thereof by 120% [the level of debt service coverage]....Airline shall also pay to City, commencing on the DBO, an annual Operations Charge on a monthly basis sufficient to reimburse the City for the cost of furnishing services.

A significant difference between the Old Terminal leases and the CPTC leases is to be found in the section covering concessions. The airline leases cover the subject of concessions at some length because, as a primarily residual-cost airport, Hartsfield credits a large percentage of "inside concession" revenues against airline rental payments. Specifically:

> of the fees paid to the City by the Principal Concessionaire for the inside Concessions...the City shall, in the following order: (i) retain the City Annual Retention Amount; (ii) credit the Contracting Airlines with such fees in excess of the the City Annual Retention Amount up to but not exceeding the Airline M&O Recovery Amount, and (iii) credit the Contracting Airlines with any such fees in excess of the City Annual Retention and the Airline M&O Recovery Amount up to, but not exceeding the Airline Annual Retention Amount. Thereafter, fifty percent of the fees paid to the

> City by the Principal Concessionaire for the Inside Concessions...shall be credited to the Contracting Airlines ....the credits provided for herein shall be applied by reducing the rentals and charges payable by the Contracting Airlines...

The City reserves for itself all rights with respect to outside concessions, such as parking, car rental, etc.

The use agreement is similar in spirit to the CPTC lease, in that much of the revenues collected from airlines, in the form of landing fees, are designated to amortize debt on capital improvements (these revenues are also used to pay operating expenses for the airport, etc.). The landing fee consists of:

(i) a Basic Landing Fee of sixteen cents per each one thousand pounds of maximum gross landing weight of the aircraft,

(ii) an Initial Field Improvements Landing Fee covering improvements to the airfield made between 1967 and 1972, and

(iii) an Additional Field Improvements Landing Fee covering any subsequent capital improvements (including land acquisition). Any State or Federal grants-in-aid, as well as any land rentals received from a party other than a signatory airline, are to be credited against Field Improvements Landing Fees payable by the signatory airlines.

Before the opening of the CPTC, there was no Additional Field Improvements component to the landing fee. Instead, the use agreement contained a provision for a Supplemental Landing Fee computed by multiplying $3539 per year by the number of gates in the old terminal leased to each carrier under its existing lease. This amount was

stated to be "in consideration of the installation by the City in the Existing Terminal Area of aircraft loading positions and common use access to such loading positions."[7] These costs for the CPTC are, of course, now covered in the lease agreements.

Termination

The CPTC lease gives the city the right to terminate the lease if the airline defaults on certain parts of the agreement. The following are considered events of default by an airline:

(1) failure to make a past due rental payment after receiving fifteen days' written notice from the city

(2) failure to observe terms, covenants, or conditions of the lease agreement, even after thirty days' written notice from the city of such failure;

(3) filing of a petition of bankruptcy by the airline or assignment of substantially all of its assets for the benefit of creditors.

This last, of course, has been called into question by the events of the Braniff bankruptcy, and it is a matter of some concern to the Aviation Department at Hartsfield because of the current difficulties of Eastern Airlines.

Eastern has been in an uncertain financial state for some time, and it contributes around twenty-five percent of the airport's revenues. An Eastern bankruptcy could have a disastrous effect on debt service coverage. This fact prompted airport officials to look more closely at their sinking funds. The investigation showed that a large reserve currently exists in the sinking funds, due to the buying back of revenue bonds and the placing of extra revenues in the sinking fund accounts. The airport management feels that they could defer

payments into the sinking fund for a period of two to two-and-a-half years without violating bond covenants. They hope that this would be enough time to regain control of Eastern's space (should the bankruptcy court choose to tie it up) and re-lease it.[3]

The airlines have the right to terminate the lease under the following conditions:

(1) the airline is permanently deprived for any reason beyond its control of the rights and authorizations necessary to operate its air transport business at the airport;

(2) the airport is permanently closed to flying in general or to flights of the airline for reasons beyond the airline's control;

(3) the city defaults on the agreement in one of the following ways:

(a) failure to observe the terms of the lease agreement;

(b) closing of the airport to flying, for reason other than those beyond the city's control, for more than ten days;

(c) depriving the airline of its rights ot occupy and use the leased premises for a period greater than ten days;

(d) depriving the airline of its rights under the use agreement for a period in excess of ten days.

The airport use agreement can be terminated by the city under any one of the following conditions:

(1) the airline fails to pay rentals or fees when they fall due;

(2) the airline files a voluntary petition in bankruptcy or makes a general assignment for the benefit of creditors;

(3) the airline is permanently deprived of the power and privileges necessary for the conduct of its business;

(4) the airline abandons service to the airport for sixty days or more, except for reasons beyond its control.

The airline may terminate the use agreement under any one of the following conditions:

(1) it is permanently deprived of the power and privileges necessary for the conduct of its business;

(2) breach by the city of any of the covenants of the agreement;

(3) continued failure by the city to maintain and operate the aircraft facilities "in a reasonably satisfactory manner";

(4) operation of the airport for the accommodation of air traffic other than commercial airline traffic to the extent that commercial airline traffic is substantially restricted;

(5) the airline abandons service to the city for sixty days or more (note that terminating the Use Agreement does not have an effect upon the Lease Agreement for Contracting Airlines; their obligations to pay rent are the same).

Provision (4), above, could be a source of conflict in the future. With today's airfield capacity problems--of which Hartsfield had direct experience in the Summer of 1984, before the opening of the fourth runway--commercial air carrier traffic is bound to be restricted, eventually, even "substantially restricted." If the airport authorities decide that air transport is best served by allowing non-commercial non-air-carrier traffic to land, it may not have the

flexibility to do so. This clause may also fuel long disagreements and court battles about what constitutes non-air-carrier traffic and, also, what constitutes restrictions by such traffic of commercial air carrier operations.

Another point of interest in the termination clauses is that the airline no longer has the right to terminate its lease if the use agreement is terminated "for any legal reason", as was true under the old leases. The airlines, therefore, can voluntarily abandon service to the city and walk away from the use agreement, but not from the lease agreement. An example is Frontier, a Contracting Airline which no longer serves Atlanta, but sublets its terminal space to Delta. The airport is thus somewhat protected from financial instability brought on by deregulation.

Majority-In-Interest Clauses

The CPTC lease, because it was written to insure the financing of enormous capital expansion, is a lengthy and complex document. It creates a strongly interdependent relationship between the airport and the airlines--especially Eastern and Delta, which contribute approximately fifty percent of total airport revenues. As would be expected, then, Atlanta's lease and use agreements both have majority-in-interest (MII) clauses.

The lease describes an MII as:

> fifty-one percent or more of the Contracting Airlines, which have also leased seventy-five percent or more of the total Aircraft Parking and Ramp Area square footage exclusively leased to all Contracting Airlines and seventy-five percent or more of the total Exclusive Leased Premises in the Landside Terminal Buildings and the Concourse Buildings leased to all Contracting Airlines.

The use agreement describes an MII as:

> any four or more of the Atlanta Airlines which together paid at least ninety percent of the total Basic Landing Fees during the preceding twelve month period.

(Table 4-2 is a list of the specific rights and responsibilities of the majorities-in-interest at Hartsfield).

It is important to note, however, that the city has reserved the right to use much of its own discretion in further airport development. Specifically, although any major airfield improvement requires MII approval under the terms of the use agreement, another clause appears in the agreement which states:

> The parties hereto do hereby agree in principle to the Airport Land Use Plan as presented [in the named document]. Said plan is further acknowledged to be the guide for the City and the Atlanta Airlines in the proposed development of the existing Airport.

Also, a requirement for MII approval of major development of terminal or landside is conspicuously absent from the CPTC lease. A clause does appear, however, which states:

> City reserves the right to further develop or improve the Airport and/or aviation facilities in general and all roadways, parking areas, terminal facilities, landing areas and taxiways as it may see fit, so long as such developments and improvements do not adversely affect the use of the Leased Premises by Airline for the purpose outlined ...hereinabove and are not in conflict with the provisions of this Agreement.

<u>Access for New Entrants</u>

Airport officials are aware that long-term leases are somewhat suspect in the eyes of the federal government because they can be seen as a means for keeping out new entrants by tying up available space.

TABLE 4 - 2: AREAS IN WHICH MAJORITY-IN-INTEREST (MII) APPROVAL OF CONTRACTING AIRLINES IS REQUIRED

In Lease

- Authorization of use of Landside Terminal Buildings for loading unloading of passengers from "remote gate" operations
- Imposition of a toll, by the city, for use the building rail system by airlines or their employees, passengers, guests, patrons, invitees, or suppliers of materials
- Construction of a hotel facility "within, on or over the Project"
- Replacements and repairs of basic systems and their components in the terminal area
- MII is responsible for development of standards specifications and procedures for levels of staffing, maintenance and operations of the building rail system
- Tenant finishes and decor of the principal concessionaire
- Concurrence in the buying out of the principal concessionaire, should the city opt to do so on the date named in ;the lease agreement
- Matters involving insurance coverage for the CPTC
- The level of fire and police protection to be provided by city for terminal building area
- The exercise of the principal concessionaire's rights to supply concession services to the jointly leased areas of the terminal buildings outside of designated concession areas
- Designation of an airport consulting firm to determine if the construction of the additional FIS Facility is required
- Changes in the sequence of gate assignments to international arrivals at the Future City FIS Facility (when it is built)
- Designation of concessions as inside or outside concessions
- Costs and financing arrangements for many substantially-sized capital projects

In Use Agreement

- Any major airfield improvement, including land acquisition.

Although there are no specific legal requirements for airports to accommodate new entrants, an aspiring entrant to a market could bring court action against existing lessees and the airport alleging restraint of trade. Therefore, there is a policy at Hartsfield to try and accommodate new entrants by writing some flexibility into leases. The wording of these clauses, however, is not strong and exists more as a statement of intent than as an enforceable policy:

> Subject to its own requirements, Airline agrees to cooperate with City in making space available in the Terminal Building Area to any airline or air carrier or other party which may become certificated or otherwise authorized under applicable law to provide passenger air transportation to/from Atlanta, Georgia, to insure that space will be provided for any such airline or air carrier on a fair and equitable basis.

Elsewhere in the lease, the clause appears:

> Any airline, air carrier or other firm engaged in the air transportation of persons, property or mail which is authorized under applicable law to serve Atlanta, Georgia may become a Contracting Airline by entering into an agreement substantially the same as this Agreement.

The primary means, however, of accommodating new entrants is through sublease agreements. For the present, at least, this method has been adequate for allowing new carriers access ot the airport. The clause covering subleasing is as follows:

> Airline may sublet its leased Premises, in whole, or in part, to any other air carrier, or air carriers, authorized to offer scheduled service at the Airport; provided, that unless the City consents in writing to release Airline therefrom, which consent shall not be unreasonably withheld, no such sublease shall serve to release Airline from any of its obligations, duties or responsibilities with respect ot such Leased Premises under this Agreement, and provided, further, that no such subletting shall be at a rental charge in excess of that charged to Airline by the City under this Agreement, plus the unamortized investment of Airline in

> improvements...installed by it at its expense, unless such excess be assigned to the City as additional rental under this Agreement...

The issue of finding room for new entrants is not yet a major one, largely because, unlike several other major airports in the United States, room for terminal expansion still exists at Hartsfield. Certain areas of aircraft ramp have been designated as the site for the "Future City FIS [Federal Inspection Services] Facility", which would be built as an addition to the present FIS facility, and which would constitute seven additional gates. In addition, a future fifth concourse is part of the Master Plan, and land currently rented by Eastern Airlines for remote apron space and a ground services and equipment area, may be repossessed by the city upon twelve months' written notice for this purpose.

Because of this ability to expand, the issue of a gate recovery "use-it-or-lose-it" clause is non-existent. There is also an acknowledged dependence upon the airlines, especially Delta and Eastern. The airlines prefer to have complete control over their gates and it is in the airport's interest to keep the airlines happy, not to mention that having an airlines' gates in proximity to one another facilitates transfers--an important consideration in Atlanta.

## Conclusion

The objectives of the Aviation Department are quite clear. The airport is a vital part of the region's economy--as mentioned before, the state's largest non-federal employer--and has recently built the largest air terminal in the world. The main goals for the airport as evidenced in the lease agreement are to guarantee the financing for

this terminal and to plan ahead for Atlanta's continued prominence in the air transport system. The lease is long and highly complex in its effort to insure that these goals are met, and this is most likely a matter of necessity.

One can also see the importance of the airport's residual-cost structure. The airlines are carrying major parts of the financial burden of the debt on the new terminal. They would naturally insist upon having that burden alleviated wherever possible.

Hartsfield is fortunate in not having the kind of environmental pressures upon it that other airports, notably in the Northeast, are experiencing. There are some complaints about noise, and a few of these have gone to court, but the airport is largely free to develop and grow as it sees fit, at least for the foreseeable future.

Because of its standardized lease and its extensive financial interdependence with the airlines, however, the airport lacks a great deal of flexibility in being able to face the possible problems of the future. The significance of this will most likely be tested first by airfield capacity becoming severely restricted. This will cause competition for slots among the airlines at the airport to become more fierce, and the rights of use agreement signatory carriers over non-signatory carriers may be cited by the carriers to justify their claim to first priority for slots. Also, of the twenty-two carriers serving Atlanta, only eight have lease agreements with the city. Most of the others are sublessees and are dependent upon the goodwill of the eight Contracting Airlines, who may sublease or not, entirely at their own discretion. How much power the airport will have to respond to such situations for the benefit of the region and the travelling public remains to be seen.

# CHAPTER FIVE: KANSAS CITY INTERNATIONAL AIRPORT

Kansas City, Missouri acquired its first airport in 1926 with the purchase of what is now Municipal Airport. Municipal is situated a short distance from the downtown business district in a bend of the Missouri River, and, because of this location, the runways (the longer one is seven thousand feet) could not be extended. It was, therefore, determined very early that a new, enlarged airport would be needed. In 1953 five thousand acres, located approximately fifteen miles from the downtown area, were acquired for a new airport. A runway and some apron space were built, as well as overhaul base facilities which were occupied by TWA in 1957. TWA still maintains a major maintenance and overhaul base at the airport, and it was the prinicpal airline in Kansas City at that time. It was also the principal airline supporting construction of Kansas City International (KCI) Airport.

In 1966, a $150 million bond issue was approved by the city voters, and development of the new airport was launched. Bids for construction were let in 1968, and in November of 1972, all scheduled airline operations were transferred to KCI from Municipal Airport.

Kansas City International was classified as a large hub in 1970. The rate of traffic growth, however, began a downward trend in 1979, and it was reclassified as a medium hub in 1980. The facility has a design capacity of twelve million passengers per year, but only handled 5.2 million in 1981. This figure was a decline from 5.9 million travellers using the airport in 1979. The airport had registered net passenger gains of only twenty-seven percent between 1970 and 1980, and aircraft departures had dropped nine percent between 1978 and 1980. This drop was probably caused by both the

recession of that time and the changes, brought about by deregulation, in airlines' route networks.

The traffic decline was also tied to the decline of Braniff Airlines, which was then a major KCI tenant, and its decision to cut its daily flights at the airport in half. The result for KCI was two consecutive years of declining traffic.[1]

Traffic growth has recovered substantially since that time, however. For example, In May, 1984, KCI had five large aircraft operators, two small aircraft operators, and four cargo carriers which were not serving the airport a year earlier.[2] Some of these new entrants have since departed Kansas City, but traffic there has maintained an increasing rate of growth.

Kansas City serves as a gateway for portions of six states: Missouri, Iowa, Nebraska, Kansas, Oklahoma, and Arkansas, and the airport sees itself as a viable and desirable alternative to such airports as Denver's Stapleton International and St. Louis' Lambert International. It's location is just as convenient, if not more so, as that of other midwestern airports, and it has the ability to expand by adding more runways and building a fourth terminal. The airport site currently covers roughly six thousand acres, with plans for possible expansion to ten thousand acres in the future. Even without this ability to grow, congestion is not a problem for KCI. Air operations are at approximately sixty percent of runway capacity, passenger activity runs at about forty-two percent of terminal capacity, and entry road traffic is estimated at thirty-three percent of capacity.[3]

In addition to these advantages over crowded Midwestern hubs, KCI is fifteen miles from downtown Kansas City and in a very sparsely populated area. This fact allows the airport to escape most of thenoise and environmental pressures other airports experience. One

airport official observed, "The corn and soybeans don't complain about noise." Commercial development is slowly creeping out toward the airport, but the city is working to obtain noise easements over any nearby development which may materialize.[4]

It is apparently the airport's central location and its growth potential which has caused enplanements to rise in the last year. The entry of Eastern Airlines into the market in late 1983, with plans to build an important hub at KCI is the most significant factor in this growth. Eastern is now developing KCI in a way that TWA had, apparently, originally planned when it established its major overhaul base there and, later, became instrumental in the construction of the new airport. Eastern's hub at KCI has had a significant impact upon the airport. Because the reasons which caused Eastern to choose KCI are good examples of why it can be an attractive airport to carriers, they will be described in some detail.

Most other U.S. airlines had a midwestern hub, already, with Eastern being the major domestic service exception. The midwest, then, is a dense corridor for airline traffic and is a very competitive market. Eastern's objective for some time had been to maximize it's route structure by searching for a mid-continent hub that would allow it to connect the densely populated Northeast and Great Lakes areas through to the West. St. Louis was first considered, but TWA and Ozark began to add flights there and posed too strong a competitive factor.[5]

In searching for its central hub, Eastern's broad considerations were:

(1) current total traffic in and out of the city,

(2) current total number of departures of non-stop flights from the city.

They sought a central location, a dense local traffic base, and adequate facilities with an ability to accommodate growth. From this beginning they narrowed the field by further examining each candidate city for:

(1) potential for Eastern to dominate the market (KCI had lost Braniff, with TWA and United also slowly withdrawing),

(2) amount of low-cost competition,

(3) flight range of Eastern's narrow-bodied aircraft (geography, again),

(4) population trends (Kansas City is a growing and prosperous city),

(5) income per capita,

(6) the ability to schedule west-east traffic and land in an acceptable time window at the hub (another geography factor).[6]

Of the cities considered, Kansas City best fit the desired description. Eastern entered the airport in November, 1983, and the subsequent effect upon air traffic has been significant.

By the end of November, 1984, a record number of passengers had already been handled by the airport for calender year 1984. The 5,950,057 passengers represented a 31.57% increase over levels for the same period in 1983. Concurrently, air carrier operations increased 43.95% and total operations over all categories of aircraft increased 35.52%.[7] That this is largely attributable to Eastern can be seen from the fact that only two airlines besides Eastern have seen a rise in passengers at KCI in 1984: American and Delta.

The nature of the traffic has changed as well. The major portion of the more than thirty-one percent rise in passenger traffic is from

transfers. In 1983 transfers were twenty-seven percent of the total--this was pre-Eastern--and currently, sixty percent of Eastern's traffic, alone, is connecting. Transfer passengers have increased at a rate of roughly twice as much as origin-destination passengers.[8]

The changes of the last few years at Kansas City International have been attributed largely to deregulation. James Gerner, Assistant Director of Aviation, pointed out that, in 1972, when the airport was opened, the city was being served by a stable number of eight airlines. Since 1978, this number has grown to the neighborhood of twenty-five carriers, and, he estimated, some kind of turnover takes place roughly every ninety days.[9]

Members of the Aviation Department also acknowledged that the fluctuations of the last seven years have created competition with other airports--mainly St. Louis--over which city will serve as mid-continent hub for which carriers. Clearly, KCI would suffer from an event such as a bankruptcy of Eastern Airlines, and the airport would probably respond by trying to attract a large carrier away from one of the highly congested Midwestern airports by marketing the lack of delays and congestion at KCI.[10]

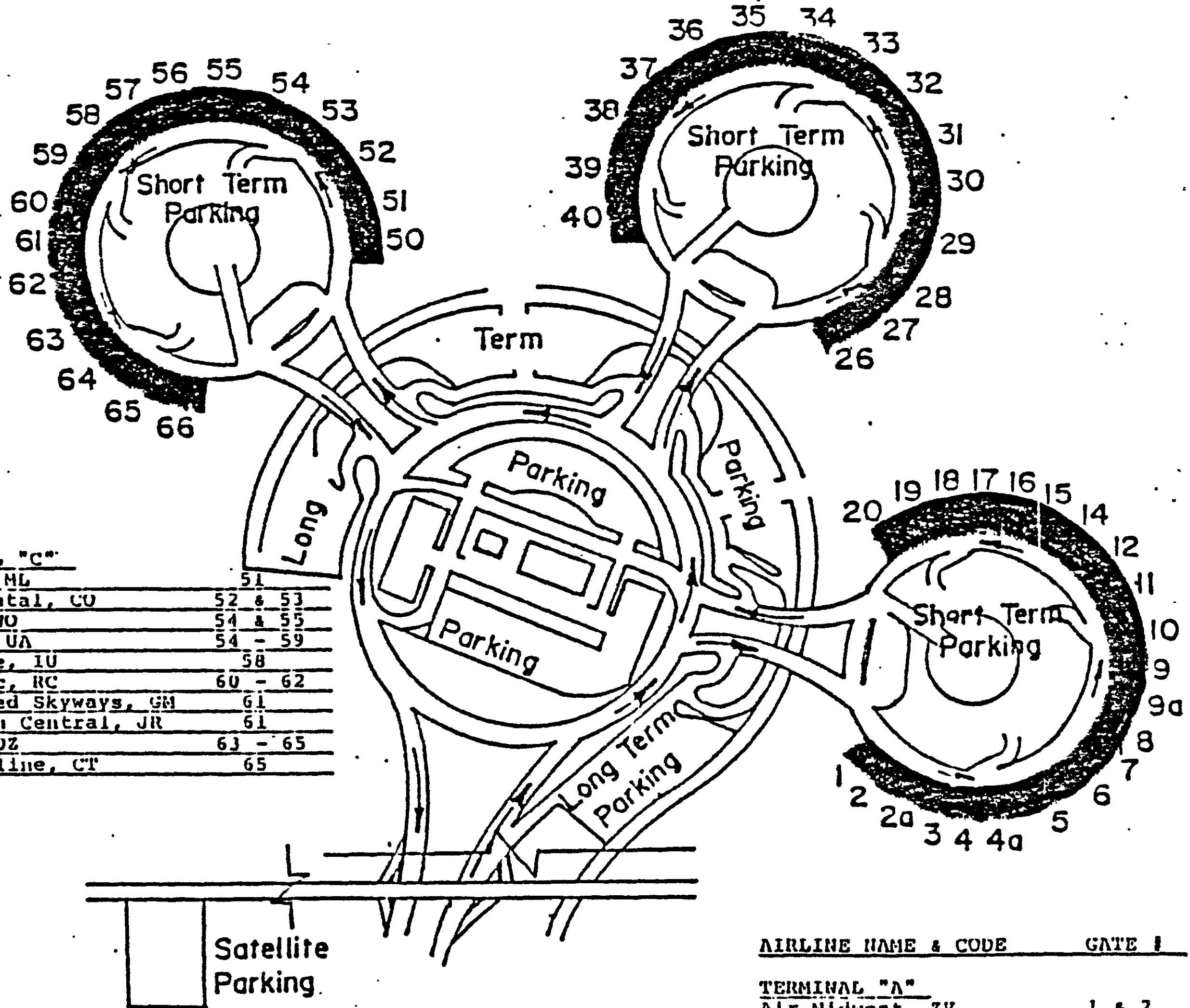
However, James Mallon, Air Service Specialist at Kansas City International, pointed out:

> We don't want to get into the position of a Denver or a Chicago or a St. Louis. We want to have good service for our community, which comes from having a hub which feeds in from everywhere else, so we can give our travellers a better choice of flights in and out. But we don't want to grow to a position where we are congested, and it is a problem or a real chore to use the airport.[11]

Given the changes, over recent years, in the air service at KCI, one might expect the leases and use agreements to have changed, as well. This, however, is not the case. The airport's uniform Lease and Use Agreement was first written in 1969 in anticipation of the need for

# KANSAS CITY INTERNATIONAL AIRPORT

| TERMINAL "B" | |
|---|---|
| TWA, TW | 27 - 35 |
| Western, Wa | 32 |
| Capitol Air Service, RX | 36 |
| Delta, DL | 37 - 39 |




| TERMINAL "C" | |
|---|---|
| Midway, ML | 51 |
| Continental, CO | 52 & 53 |
| World, WO | 54 & 55 |
| United, UA | 54 - 59 |
| Midstate, IU | 58 |
| Republic, RC | 60 - 62 |
| Scheduled Skyways, GM | 61 |
| American Central, JR | 61 |
| Ozark, OZ | 63 - 65 |
| AAA Airline, CT | 65 |

| AIRLINE NAME & CODE | GATE # |
|---|---|
| TERMINAL "A" | |
| Air Midwest, ZV | 1 & 2 |
| Eastern, EA | 3 - 8 |
| Pan Am, PA | 8 |
| Southwest, WN | 9 |
| America, AA | 11 & 12 |
| Frontier, FL | 17 - 20 |
| Northwest, NW | 16 |
| US Air, AL | 17 |

debt-service coverage for the revenue bonds issued in 1967. Except in a few instances of additions or revisions to a particular clause, the lease and use agreements have not changed at all.

The Lease and Use Agreements

Kansas City International is a compensatory airport, and the lease agreement states, that on an annual basis:

> rental rates shall be revised and adjusted to reflect the City's changing experience of expense of the demised premises so as to provide for the payment by Airline to the City of rental based upon compensatory rental rates for the space leased to Airline.(p. 8)

The compensatory rates include interest on investments in land, interest and depreciation on airport facilities, as well as maintenance and operations expenses. There is also a provision for "Payments-in-Aid-of-Financing", should the total of annual rentals and use-fees from the airlines be less than $7,048,989. This insures that annual sinking fund requirements can be met. The Official Statement for the 1967 bond issue notes:

> The provisions of the "Agreement for Mid-Continent International Airport Leases" constitute a non-cancellable commitment by each of the airlines to pay, so long as any of these bonds are outstanding, amounts which in the aggregate shall not be less than the cost of operation and maintenance, including deferred maintenance, of the airport, and interest and principal on these bonds.[12]

Therefore, although the airlines do not actually legally guarantee the bonds, their rental payments stand as security for the debt.

Consistent with its compensatory approach, KCI does not use concession revenues to offset and reduce airline rentals and use fees.

Interestingly, the lease supports this policy by stating the philosophical opinion that:

> other airport users and other tenants including the public must pay for their proportionate use also. The terminal building and terminal area public spaces are considered as occupied by the public as a tenant and the public will pay for this occupancy through its patronage of airport concessions which will generate income in excess of the City's cost of the space occupied by concessionaires, which excess income from concessionaires shall be considered by the City to be in lieu of rent from the public for the publicly used airport areas.(p. 14)

Because of its ability to control these funds, the airport has financed every capital investment, since original construction, with surplus airport revenues.[13]

Kansas City International was obviously in at the beginning of a now-favored trend in establishing itself as a compensatory airport in the late 1960's. How the city was able to accomplish this while, at the same time, seeking guarantees of debt coverage from the carriers can only be speculated upon. The premise that a carrier is in a weaker bargaining position if it needs the airport as badly as the airport needs the carrier is only common sense. TWA was instrumental in the construction of the airport, because its overhaul base was there and because it had plans to develop Kansas City as a hub. This may have placed the city in a stronger position, and may have influenced the writing of the lease.

It is certainly true that, in 1983, Eastern Airlines wanted to enter KCI for reasons of its own, and, therefore, although the airport's traffic had been declining, it was not forced into a position of having to bargain with Eastern. In any event, it would have been limited in its ability to do so by the following clause:

TABLE 5 - 1: CITY OF KANSAS CITY, MISSOURI

KANSAS CITY AIRPORTS FUND

STATEMENT OF REVENUES, EXPENSES AND TRANSFERS

FOR THE YEARS ENDED APRIL 30, 1984 AND 1983

| | 1984 | 1983 |
|---|---|---|
| OPERATING REVENUES (Note 5): | | |
| Field and runways | $ 4,716,912 | $ 4,303,934 |
| Terminal buildings and aprons | 7,136,211 | 6,265,635 |
| Other property rentals | 4,346,848 | 3,813,473 |
| Parking concessions | 6,310,351 | 5,455,780 |
| Air Force rentals | 2,363,524 | 2,606,005 |
| Federal grants on maintenance projects (Note 4) | 3,850,323 | - |
| Other | 64,249 | 72,313 |
| | $28,788,418 | $22,517,140 |
| OPERATING EXPENSES: | | |
| Salaries, wages and employee benefits | $7,797,348 | $ 7,805,473 |
| Materials and supplies | 1,316,130 | 1,473,879 |
| Utilities | 3,579,312 | 3,471,929 |
| Interfund payments (Note 7) | 353,123 | 329,085 |
| Other contractual services | 1,804,084 | 2,085,878 |
| Repairs and maintenance (Note 4) | 6,009,777 | 1,202,531 |
| Bad debts | 63,512 | 930,698 |
| Other | 175,019 | 185,739 |
| Depreciation on properties acquired from- | | |
| City funds | 4,449,521 | 4,087,128 |
| Contributions and grants | 1,045,515 | 864,051 |
| | $26,593,341 | $22,436,391 |
| Operating income | $ 2,195,077 | $ 80,749 |
| OTHER INCOME (EXPENSE): | | |
| Interest on investments | $ 2,192,127 | $ 3,074,843 |
| Bond interest and fiscal agent fees | (1,741,980) | (1,826,117) |
| | $ 450,147 | $ 1,248,726 |
| Income before operating transfers | $ 2,645,224 | $ 1,329,475 |
| OPERATING TRANSFER FROM GENERAL FUND | - | 254,325 |
| Net income | $ 2,645,224 | $ 1,583,800 |

Source: Kansas City Aviation Department

Interestingly, the lease supports this policy by stating the philosophical opinion that:

> other airport users and other tenants including the public must pay for their proportionate use also. The terminal building and terminal area public spaces are considered as occupied by the public as a tenant and the public will pay for this occupancy through its patronage of airport concessions which will generate income in excess of the City's cost of the space occupied by concessionaires, which excess income from concessionaires shall be considered by the City to be in lieu of rent from the public for the publicly used airport areas.(p. 14)

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It is certainly true that, in 1983, Eastern Airlines wanted to enter KCI for reasons of its own, and, therefore, although the airport's traffic had been declining, it was not forced into a position of having to bargain with Eastern. In any event, it would have been limited in its ability to do so by the following clause:

> The City covenants that, during the term of this lease, all scheduled airlines serving the City will be treated equally in that all rentals and fees to all airlines will be compensatory and that all airlines, whether now serving the City or certificated to serve the City at some future date, will be required to execute leases providing for minimum rentals, use-fees and Payments-in-Aid-of-Financing with the same then current economic burden effect as those being executed by the airlines presently serving the City.(p. 12)

KCI veers somewhat from the compensatory approach in the sections of the Lease and Use Agreement which cover airfield use. Strictly speaking, these sections need not be included at all, as Section 204, entitled "Access" grants "privileges of ingress and egress" to and from leased premises to the employees, aircraft and equipment, passengers, suppliers, etc. of the carrier. The carrier is thus guaranteed use of the airfield (how else could an aircraft gain access?), and, because the carrier does not lease portions of the runways and taxiways, the airport could set use fees (landing fees) unilaterally.In fact, however, the carriers agree to pay "compensatory fees" of a stated amount per thousand pounds, which are revised annually. This clause also states that this rate is extended to revenue flights--excluding, apparently, non-revenue landings of aircraft. Further, these fees are not actually compensatory. The same section, dealing with use fees, M states that fees collected from users of the field who are not scheduled carriers (e.g. general aviation, charters):

> shall be applied to reduce the amount of field and runway expenses to be collected from the scheduled airlines through use fees.(p. 9)

The carriers seem to have a much stronger presence in this section of the agreement. One possible explanation for this is that landing fees may have represented a much larger proportion of their airport expenses than did terminal rents, at that time.

KCI also has a separate Use Agreement with carriers who serve the airport but do not lease space directly from the city. It grants the right:

> to land and take off the Airline's aircraft, at and from the Airport and to process its arriving and departing passengers thereon in accordance with the terms and conditions hereinafter set out. (p. 1)

The carrier agrees to pay a landing fee that is equal to that of the tenant carriers plus fifteen percent, and to pay, either directly or through the airline from whom it subleases, any other charges for such services as inter-terminal transportation or gate security.

Majority-In-Interest Clauses

As might be expected from its reliance on the carriers for debt service coverage and for revenues to cover its other expenses, Kansas City International has a majority-in-interest clause in its lease. An MII is defined as those carriers with more than fifty percent of the landed weight for the preceding six months. In no event however, can an MII be made up of less than one third of the leasing carriers. The airport MII is only granted one right in the lease agreement, but this is an important one (it is also the one that is most commonly associated with MII clauses in airport lease agreements). The section in question states:

> the City and the scheduled airlines serving the Airport ...agree to discuss proposed improvements in an effort to arrive at a mutually satisfactory agreement with respect to physical plans and changes or adjustments in use fees or rentals. In the absence of such mutually satisfactory agreement between the City and the majority in interest of the scheduled airlines, the City shall not be obligated to make said capital improvements but, if it proceeds with the

> improvements without the consent of the majority in interest of the scheduled airlines, the cost of such improvements shall not be taken into consideration in determining said use fees and/or rentals.(p.14)

Because KCI Airport has not needed to make any extensive investments in expansion since the original construction, the MII clause has not posed any major restrictions upon airport planning. It is not likely to do so in the near future, either, as the airport is not operating near capacity levels and has no immediate need for major expansion.

Length of Lease Term

Another lease provision which grows directly out of the arrangements for bond financing is that of the length of the lease term. The leases originally signed in 1969 went into effect on June 1, 1970, and are to terminate on May 31, 1998--a term of twenty-eight years (the airlines, then, were required to make Payments-in-Aid-of-Financing some two years before actually moving into the new facility). The lease is set to coincide with the maturity of the 1967 Revenue Bonds, and any new leases which have been entered into since 1969 also terminate in 1998. This is because leases are specifically written to honor the city's covenant that:

> as long as any of said revenue bonds were outstanding, it would have scheduled airline agreements for payment of rentals, use fees and Payments-in-Aid-of-Financing applicable to the construction program then underway...of $7,048,989 annually.(p. 12)

When the bonds are no longer outstanding, the lease states that the minimum Payments-in-Aid-of-Financing will cease.

The lease term was established, at the time, as the best way to obtain favorable interest rates on the bonds. Airport administrators at KCI continue to feel that long-term leases would be required for such financing, because long-term leases are less risky.[14] Given the changing fortunes of the airport over the last decade, the perception of risk may be realistic, but it is also true that Kansas City is a growing and prospering community with a strong origin-destination traffic factor. The trends currently observed in the airport revenue bond market indicate that KCI might find that it is less dependent upon long-term leases than it supposes. Because the city has not sought financing from the bond market sine 1967, however, this hypothesis has not been tested.

The term of the airport use agreements with carriers not renting from the city is, by contrast, only one year. This agreement contains no stipulations for Payments-in-Aid-of-Financing, and the airport does not depend upon this revenue to meet its debt obligations. Therefore, the agreement allows for more flexibility by its short term while establishing a formal relationship between the non-leasing carriers and the airport. Of course, it is also true in this case that the airport would have more influence over its own landing fees by not entering into such agreements, at all.

Access for New Entrants and Gate Recapture

In addition to the formal recognition given the non-leasing carriers in the Use Agreement, the lease recognizes them in other ways. The Lease and Use Agreement contains several provisions which deal with the needs of new entrant carriers. For instance, in the leasing of vacant terminal space, the lease stipulates that resident

carriers will have the opportunity to make their needs known, but it does not give right of first refusal of the space to any carrier.Also, the Use Agreement states the airport's expectation that the newly entering carrier will "make arrangements with a certificated scheduled air carrier for passenger terminal building space and aircraft apron space."(p. 1) In turn, the lease stipulates that a carrier can sublease, with the consent of the Director of Aviation. (p. 25)

In 1984, some new language was added to the "Assignment and Subletting" section of the lease which gives a stronger bargaining position to potential new entrants. The new paragraph states:

> If Airline's sublessee requires ground handling of its aircraft and/or processing of its passengers and their baggage, it shall have the right to contract with Airline or any other party for such services and shall not be required to secure such services from Airline, as a condition of entering into the sublease.(p. 25)

Closely related to the issue of accommodating new entrants is, of course, the issue of control over gates. The KCI lease has always contained a paragraph, regarding apron space, which states:

> When Airline has no aircraft requiring use of the apron loading position, the City may allow others to use the apron as circumstances and the public interest require. (p. 3)

Stronger language was added to this section in 1984, which requires that the carrier minimize its time of usage of this space and remove its aircraft promptly (when not being loaded or unloaded) if the airport notifies it that the position is required for use by others. The city promises, "where practicable", not to require a carrier to accommodate an airline with directly competing service.

The city recognizes in the lease that the leasing carrier should receive compensation for use of its gates and apron space. In addition, again in recently added new language, KCI reinforces its stand on gate-access by stating:

> If a mutually acceptable method and amount of compensation for such use cannot be agreed upon between Airline and the aircraft operator requiring secondary use, then City reserves the right to determine what a fair and proper compensation method and amount should be and impose it on the parties. (p. 4)

This "sharing" clause has never had to be enforced by airport administration, as carriers have been able to negotiate agreements among themselves.

In a further move to strengthen its control over gate positions, the airport added a "Level of Service" section to the lease in 1984 which specifies a level of gate utilization which must be maintained. In part, this section reads:

> Any gate position shall be deemed underutilized if the average weekday flights of Airline's aircraft arriving at that gate position is 35% less than the then current average gate utilization of all scheduled air carriers operating aircraft of a similar size and having similar agreements hereto with the City.
>
> If, at any time, one or more of Airline's gate positions is underutilized, and remains so for a period of six months, and any other scheduled air carrier expresses its willingness to utilize the gate(s) at a higher level than the current average utilization of all scheduled air carriers operating aircraft of a similar size, then that carrier shall have the right to acquire Airline's improvements in the gate position(s) and enter into an agreement similar hereto for the use and occupancy of the premises as a substitute for Airline. (p. 5)

The gate recovery clause is only found in leases entered into in the last year. It will be added to Eastern's lease in an amendment which will also lease four more gates to that airline. The two other carriers which had signed this clause have now left KCI: America West and the new Braniff. The Airlines have, so far, not objected to this clause, perhaps because it poses no problem to any of them at their present level of service.[15]

The existence of these provisions in the lease is somewhat surprising in view of the fact the KCI has no history of constrained and scarce gate positions. The airport has also not made a practice of interfering in inter-airline agreements. As Assistant Director of Aviation Gerner pointed out, the city built the facilities that the carriers were willing to pay for and allowed them to determine for themselves whether they had excess space or not. In his opinion, the reason for adding specific "use-it-or-lose-it" language, now, is that "it became popular" in the industry.[16]

Termination

The final section of the lease which must be considered is that which deals with termination of the agreement in its entirety--either by the city or by the airline. In brief, the city has the right to terminate if:

(1) the carrier files a voluntary petition of bankruptcy or assigns its assets for benefit of creditors;
(2) the carrier is judged bankrupt as a result of involuntary bankruptcy proceedings;
(3) a court of law takes jurisdiction as a result of a Federal reorganization act;
(4) a receiver of the carrier's assets is appointed;
(5) the carrier voluntarily abandons conduct of its air transport business at the airport;
(6) the carrier breaches any of the lease covenants and fails to remedy the breach.(p. 26)

The airline may terminate if:

(1) a court of law issues an injunction preventing or restraining use of the airport for air transport purposes for a period of more than sixty days;

(2) the city breaches any of the lease covenants and fails to remedy the breach;

(3) due to war, earthquake, or other casualty, the airline is unable to use its leased premises for a period of more than ninety days;

(4) an obstacle is erected in the vicinity which would violate minimum safety standards for the operations of the carrier;

(5) a governmental authority acts to take control of the leased premises which prevents the carrier from conducting its business;

(6) a part of or all of the airline's leased premises are taken by eminent domain;

(7) the carrier's certificate of public convenience and necessity is suspended. (pp. 26,27)

In addition, a restriction is placed upon the carrier's right to terminate which protects the city's ability to meet its debt obligations:

> Airline shall not exercise any cancellation right set forth above unless, prior to such cancellation, the City has in hand contracts and leases of equal value to those Airline seeks to cancel from another scheduled airline or from the remaining scheduled airline tenants at the Airport, but this limitation on cancellation shall apply only so long as Kansas City General Improvement Airport Revenue Bonds, Series September 1, 1967, shall be outstanding.(p. 27)

The most recent example of this last clause being invoked is the case of America West Airlines. The carrier has not served the airport since Autumn of 1984, but continued paying rent until February, 1985, when the lease was transferred. [17]

The city also reserves the right to terminate both the lease and the use agreement if the Civil Rights - Equal Opportunity clause of

either is violated. This stipulation is stated as a part of those clauses, rather than the termination section.

That four of six conditions for termination by the city deal with bankruptcy and reorganization is noteworthy, given the recent ineffectiveness of such clauses (in actual fact, Braniff's bankruptcy did not affect KCI severely because Braniff had subleased most of its gates there). The effects of these clauses under new Federal bankruptcy laws remain to be seen. Of much greater significance is the fact that carriers cannot simply abandon their leases through any of the termination stipulations.

## Conclusion

The Kansas City International Airport Lease and Use Agreement is a fascinating mixture of both currently-promoted and more "traditional" practices. The Aviation Department has observed the problems being faced by the administrators of its sister airports in more heavily-populated areas of the country and has taken steps which anticipate some of these difficulties. An example is the obtaining of noise easements, should commercial and residential development come to the area surrounding the airport. Another example is the gate recovery clause in the lease and use agreement.

Kansas City has avoided airport environmental and capacity problems because it moved its airfield away from the populated areas of the city, and even if traffic levels never rise to the point where the airport must take advantage of its capacity to expand, the move has proven to be a wise one. The airport has the advantage of considerable time-lag between the point when a potential problem is recognized (primarily from observing the experience of other airports) and the point that it reaches crisis levels.

The airport seems to have a bright future as an active hub because it is well-situated to be a mid-continent transfer point, and because the alternatives (St. Louis, Chicago, Denver) often experience delay problems. Eastern Airlines has recognized this, and, in fact, has begun to advertise the advantages of changing planes in Kansas City International over O'Hare to east-west travellers.

Because the KCI airport administrators are not ambitious to see their airport grow too large and too busy, they are less inclined to attract airlines by giving them extensive control over the terms of the lease. This accounts for much of the language of the agreements which puts the airport in a "strong" position. In fact, Kansas City International is probably even less dependent upon its residentcarriers than its administrators think it is. This will be especially true if Eastern's hubbing effort takes hold, and the hubbing momentum discussed earlier begins. Overall, KCI is probably the best prepared to face the future of the three airports examined in this study.

# CHAPTER SIX: BOSTON-LOGAN INTERNATIONAL AIRPORT

Boston-Logan International Airport is located approximately three miles from downtown Boston on a peninsula extending into Boston Harbor. With approximately twenty million annual passengers, it is the busiest airport in New England, and the tenth busiest airport in the United States. Logan has four major runways, from seven thousand feet to ten thousand feet in length, and a twenty-four hundred foot runway for general aviation aircraft.

Logan Airport was managed by the City of Boston until 1948, when the Commonwealth of Massachusetts assumed control as part of a move to expand and modernize it. The Commonwealth established the State Airport Management Board to administer the airport. In turn, the governer and legislature directly controlled the Airport Management Board. Financial support for Logan came from taxes. By the mid-1950's, however, the airport had accumulated a debt of over $42 million, and, in an effort to relieve the tax burden and remove the airport from state politics, the legislature passed the Massachusetts Port Authority Enabling Act in 1956. In 1959, the Port Authority (Massport) took control of Logan International Airport, the Boston seaport, Hanscom Field (a general aviation airport some fifteen miles from the city), and the Tobin Bridge, a toll bridge leading into Boston from the north.

Ownership of several facilities has given Massport a sound financial base from the beginning, and this has undoubtedly had an effect upon the evolution of policy toward leases and use agreements at the airport. In the early years, the toll bridge was the Authority's main income source, and it helped to support the airport and seaport. In recent years, the airport has become the primary source of revenue.

TABLE 6 - 1: Statements of Revenues and Expenses: Massachusetts Port Authority

| | Fiscal Year Ending June 30 | | | | |
|---|---|---|---|---|---|
| | 1980 | 1981 | 1982 | 1983 | 1984 |
| | (In thousands) | | | | |
| **Revenues:** | | | | | |
| Airport Properties | | | | | |
| Landing Fees | $ 17,773 | $ 18,568 | $ 20,076 | $ 22,877 | $ 24,669 |
| Parking Fees | 12,493 | 12,408 | 15,004 | 17,010 | 19,668 |
| Rentals | 19,070 | 21,102 | 21,045 | 22,096 | 23,628 |
| Concessions | 9,057 | 9,877 | 10,720 | 12,204 | 13,991 |
| Other | 8,836 | 10,821 | 11,996 | 11,600 | 12,301 |
| Total | 67,229 | 72,776 | 78,841 | 85,787 | 94,257 |
| Port Properties | | | | | |
| Maritime | — | — | — | 16,161 | 17,663 |
| Development | — | — | — | 1,357 | 1,708 |
| Total | 16,692 | 17,800 | 18,077 | 17,518 | 19,371 |
| Bridge | 5,799 | 5,923 | 5,768 | 6,201 | 6,260 |
| Facilities Management | — | — | — | — | 355 |
| Investment Income | 11,152 | 10,547 | 14,341 | 14,066 | 16,280 |
| Total Revenues | 100,872 | 107,046 | 117,027 | 123,572 | 136,527 |
| **Operating Expenses:** | | | | | |
| Airport Properties | 28,318 | 32,349 | 35,873 | 36,715 | 42,558 |
| Port Properties | | | | | |
| Maritime | — | — | — | 18,358 | 20,049 |
| Development | — | — | — | 2,657 | 2,675 |
| Total | 19,742 | 20,338 | 22,162 | 21,015 | 22,724 |
| Bridge | 2,470 | 2,694 | 2,916 | 3,239 | 3,182 |
| Facilities Management | — | — | — | — | 228 |
| Total Operating Expenses | 50,530 | 55,381 | 60,951 | 60,969 | 68,692 |
| Net Revenues | $ 50,342 | $ 51,665 | $ 56,076 | $ 62,603 | $ 67,835 |

Source: "Adjustable Rate Revenue Bonds, Series 1984, Preliminary Official Statement"

As was mentioned in Chapter Two, since deregulation in 1978, total passenger traffic has increased by 45.6% at Logan, and growth in this period has consistently exceeded that for the U.S. as a whole. The number of aircraft operations reached a new high in fiscal 1984 at332,278 operations, a fourteen percent increase over fiscal 1983. Massport expects this trend of growing numbers of operations and passengers to continue.[1]

Approximately twenty-two percent of fiscal 1984 airport revenue reflects the recovery of costs of construction and financing of improvements. These costs remain relatively fixed from year to year. Net revenues (revenues less operating expenses), however, have increased steadily since 1980 by a cumulative amount of 32.9%. This increase has come primarily from growth in parking, car rental, and other concessions. Landing fees and terminal rentals, on the other hand, are set on a compensatory basis and adjusted periodically.[2]

The airport's location on a peninsula means it is bounded primarily by the harbor, while on the land side, it is adjacent to heavily populated residential and commercial areas. The flight paths to and from Logan's runways create a serious noise problem for additional heavily-populated areas nearby. The airport's development and operations, then, are particularly sensitive to environmental factors. In the early and mid-1970's several lawsuits were brought against Massport by the surrounding towns--including the City of Boston--and by various others, among them the Massachusetts Secretary of Transportation and Construction. One such lawsuit resulted in an injunction upon the extension of two runways and the construction of a general aviation-STOL runway.[3] Because of the extreme sensitivity of the entire surrounding area to environmental issues, expansion of the airport is, most likely, a political and social impossibility, at least

for any foreseeable future. This fact has a profound impact upon all airport management practices and policies.

Partly in recognition of the price paid by surrounding communities in having a major airport in such close proximity, a 1977 amendment to the Authority's Enabling Act directed Massport to makein-lieu-of-tax-payments to the cities of Boston, and Chelsea, and further legislation in 1980 added the town of Winthrop to the list (Massport is exempted by law from paying property taxes). These payments are made only to the extent that the Authority's other financial obligations are met, and the amounts are based upon certain economic indices and upon the number of enplaned passengers at the airport.[4]

## The Lease Agreements

Logan's terminal space, unlike that of the other two airports in this study, was built in a piecemeal fashion. The airport consists of four main terminal buildings (see Figure 6-1): Southwest (Terminal A), South (Terminal B), North (Terminals C and D), and Volpe Internatinal (Terminal E). Briefly, the leasing arrangements for each terminal are as follows:

(1) Southwest Terminal is leased by Eastern Airlines, which has sole responsibility for cleaning, maintenance, and repair of the facility. The rate base for Eastern's rent includes:

(a) net ground rent,

(b) amortization of terminal costs and interest, including certain roadway costs,

(c) a share of concession income (Eastern administers concession agreements in the terminal).[5]

Massport operates the adjoining parking garage and credits Eastern with twenty-five percent of the profit from this concession. If the garage fails to show a profit in any year, the lease agreement states that Eastern will pay the amount of any net loss to Massport "in order that Authority may be saved harmless from loss on account of the Parking Garage." (Eastern lease, p. 36).

(2) There are currently no lease agreements with Delta Airlines, United Airlines, Trans World Airlines, or People Express, the carriers occupying North Terminal, although United, TWA, and Delta have had leases with the Authority in the past. Rental rates for this building are based upon a compensatory formula in which capital investment, plus interest, in the terminal is amortized over twenty-five years. The rate base also includes administrative, maintenance, and operations (AM&O) costs allocable to the terminal.[6]

(3) In 1970 a corporation, South Terminal Corporation, was formed by the then prospective airline tenants to lease and operate a terminal which was then in the planning stages. A construction and lease agreement between Massport and the terminal corporation and an interline agreement among the prospective airline tenants were written and implemented. The airlines are obligated to the Authority, under the lease, in proportion to each one's share of ownership in the corporation.

Rental for the terminal is set to reimburse Massport for its cost of constructing the terminal, plus interest on the bonds issued to finance the construction, plus an additional two percent "override". The tenant carriers have sole responsibility for cleaning, maintaining, and repairing the building. They also have responsibility for contracting all concessions (other than car rental, parking, and ground transportation) and retain all proceeds from such concessions.

Massport operates the parking garage adjacent to the terminal, but the agreement stipulates that profits above the amount of one million dollars per year are evenly shared by South Terminal Corporation and Massport.[7] South Terminal Corporation presently consists of American Airlines, US Air, Piedmont Airlines, Republic Airlines, and Northwest Orient Airlines. These carriers may each sublet termina space at their own discretion. If a carrier becomes the primary leaseholder of vacant space, however, it must join the corporation.

(4) No leases for Volpe International Terminal have existed until the present. Massport has just completed negotiating a long-term leasewith Northwest Orient Airlines for space in the building. Other carriers using the terminal pay rental rates for exclusively used space (e.g. ticket counters) based upon amortization of investment, allocated AM&O costs and payments-in-lieu-of-taxes. There are no exclusively rented gates in this terminal, and use of the common gates is scheduled by Massport. Costs of common use space are computed based upon the same expenditures (per square foot) as exclusive space. The costs are then assigned to inbound or outbound passenger activity, and a rate per passenger is derived, based upon projected traffic for the year.

The move of Northwest from South Terminal to Volpe, according to the lease agreement, is taking place because:

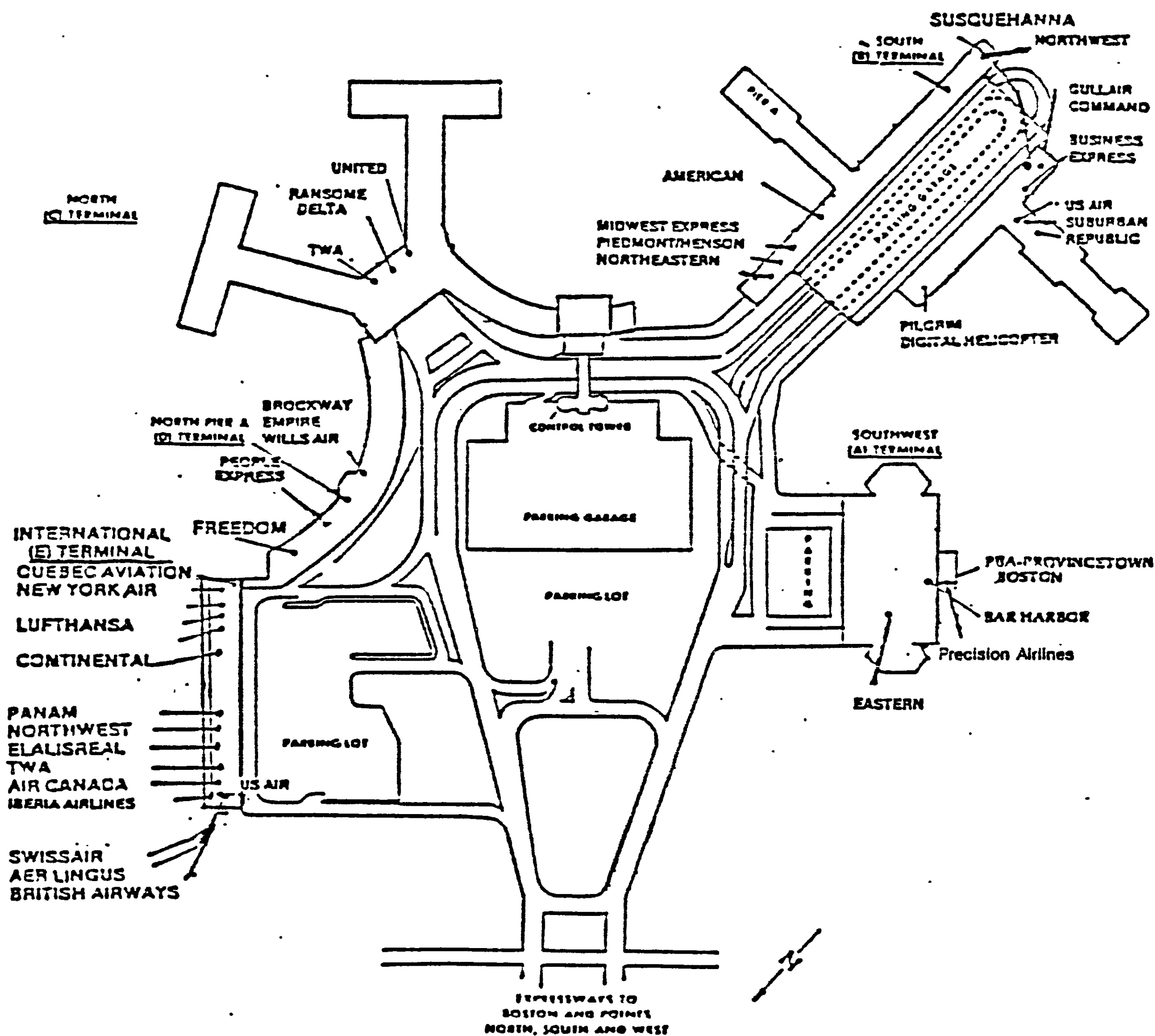
> the Authority and Airline agree that Airline's operating efficiency and the operating efficiency of the Airport as a whole will be enhanced by moving Airline's premises from Terminal B (formerly South Terminal) to Terminal E (formerly Volpe Terminal) and through assumption by the Authority of the vacated Terminal B premises upon terms and conditions that will allow the Authority to sublet the same to other air carriers selected by the Authority; (Northwest lease, p. 1).

The move will necessitate moves by other carriers now occupying space in Volpe. Massport had hoped to become a member of South Terminal Corporation in Northwest's place, and directly lease the space in South Terminal vacated by Northwest. The other members of the terminal corporation did not agree to this arrangement, however, and Massport will sublease from Northwest while, in turn, subletting again to Continental, New York Air and Pan American Airways. This level of complexity is a typical example of the problems faced by the airport administration in their efforts to efficiently manage the terminals.

An important difference between Logan and the other two airports of this study is that Logan's terminal leases are not uniform, written as they were at different times for different buildings. The leases which will be examined here are the ones currently in effect: EasternAirlines' lease of Southwest Terminal, the South Terminal Corporation lease, and the newly executed lease with Northwest Orient for a portion of the Volpe International Terminal. Some of the arrangements with the non-leasing airlines will also be described, particularly those with the tenants of North Terminal, who have exclusive use of their terminal space, despite the absence of any lease agreement. It should also be noted that all airlines in Southwest, South, and North Terminals which have not been specifically mentioned have entered into subleasing or handling agreements with the carriers named as occupying those terminals.

Use Agreements

A further difference between Logan and the other airports of this study is that Logan has never had a use agreement, nor does it include specific provisions for setting landing fees in its leases. Despite




# Logan International Airport

the span of time over which they were executed--Eastern's lease was signed in 1966, South Terminal Corporation's in 1970, and Northwest's in 1985--the clauses that mention landing fees are quite similar in all three. An example is Eastern's lease, which includes the following in a section dealing with rights of access to the premises:

> The foregoing provision of this section shall in no way limit Authority's right to impose nondiscriminatory landing fees in respect to Airline's aircraft or aircraft of Airline's sublessees and suppliers using the Airport. (Eastern lease, p. 50).

In the past, this policy regarding the setting of landing fees in leases has not been consistently followed, and examples of expired agreements from the late 1960's and early 1970's do exist which contain clauses setting landing fees. In recent years, however, Massport has adopted a great deal of autonomy in regard to its landing fees, which are calculated each year to recover the costs of providing all of the landing field facilities, including amortized capital costs, a share of administrative overhead, and in-lieu-of-tax payments. This autonomy extends largely from court decisions which resulted from litigation bythe airlines. The most important of these dealt with Bird Island Flats, an area of reclaimed tidal land at the southern end of the airport. The land was originally expected to be used for cargo storage and other support facilities, but, in 1974, the carriers, withdrew their interest in further developing the area because of declines in the air cargo business. Another 195 acres of this area had been intended for runway extensions, but these were successfully challenged on environmental grounds.

At the beginning of fiscal 1977, Massport increased the landing fee rates at Logan by 51%, in part to recover the cost of the Bird Island Flats reclamation project. Eighteen airlines filed suit

claiming that the increase was an unconstitutional burden on interstate commerce. The airlines argued that the fee was excessive because the cost allocation included expenditures for airport facilities from which they believed they derived insufficient benefit. In September of 1977, the U.S. Court of Appeals affirmed an earlier District Court decision in favor of Massport. Massport has taken this decision to be legal verification of its right to include any costs it deems reasonable in the landing fee calculation. The Court of Appeals decision stated:

> [In establishing landing fee rates] the facilities must be relevant to the operation of the Airport. And the revenues from the landing fee must be fairly consonant with the costs incurred. But within these broad parameters users share both the benefits and the costs of an airport's decisions....[9]

Further evidence of Massport's autonomy with respect to the airfield is the absence of majority-in-interest clauses. MII clauses have never been included in any agreement between the Port Authority and any carrier at Logan.

Length of Lease Terms

With regard to length of lease terms, however, the trend in favor of policies that put the airport administration in a strong management position is not as clear. The policy in this area, in fact, is markedly inconsistent. Some of the busiest carriers on the airport --Delta, TWA, and United--have no lease at all and are tenants-at-will on a month to month basis. By contrast, all three of the written lease agreements are for twenty-five year terms. This is, perhaps, not surprising of Eastern's lease and the South Terminal lease, which were both written over fifteen years ago. Northwest's lease, however, was

written in 1985, and also provides for a twenty-five year lease term.

These inconsistencies came about as a result of different historical situations. Eastern and South Terminal Corporation both agreed to amortize the costs of building new terminal buildings with their long-term leases, and the leases reflect practices which were almost universal at the time they were written, as has been noted in earlier chapters. In North Terminal, Delta., TWA, and United once had long-term leases for similar reasons. When the time came to renegotiate these agreements, Massport had decided to take a strong stand with regard to gate-recapture clauses. The carriers would not agree to these provisions, and the leases were never signed.[10] The carriers occupy North Terminal, for the present at least, as if they held an exclusive lease, but no such agreement exists. Northwest's long-term lease came about as a result of the negotiating process. Northwest has agreed to take responsibility for extensive remodeling of the space, and they have signed a comprehensive gate utilization and recovery clause. The twenty-five year lease term, while not a policy of choice for Massport, was a concession to Northwest, which wanted some guarantee that it would be able to make use of large investments in tenant finishes.[11] Massport currently holds Northwests new gates in the Volpe Terminal as Authority-controlled gates. The airport will be giving Northwest preferential use of these gates, but will be establishing the precedent of a strong gate-recapture clause. The question of whether the carriers who will move into Northwest's space in South Terminal will have exclusive use of those gates (as do the other carriers in South Terminal) or whether these will be Authority-controlled gates has not yet been answered. The decision that is made regarding these South Terminal gates will be the deciding

factor in determining whether the Northwest move and new lease represent a net gain or net loss of control over terminal space for Massport.

Access for New Entrants: Gate Utilization, Subletting and Assignment

Because of growing passenger demand at Logan, coupled with the severe environmental constraints placed upon the airport, efficient utilization of space and access for new entrant airlines are issues of great concern to the airport administrators. There is little room for terminal expansion, and this problem is complicated by the non-contiguous layout of the buildings: a gate which may be available at one building will be of little use to a carrier in another building. The recently negotiated Northwest lease contains clauses which are an attempt by airport officials to begin to deal with these issues. Before looking at that agreement in more detail, however, the assignment and subletting clauses of the Eastern and South Terminal leases should be examined. It should also be noted that neither of these agreements contains any provision for gate-sharing or gate recapture. The lessees have complete control over gate utilization.

Eastern's assignment and subletting clause is typical of such clauses, granting the right to assign or sublet, only with the Authority's prior approval, which is not to be unreasonably withheld. Eastern can sublease without prior approval if its right to serve the airport is terminated. In this case, if the Authority does not subsequently approve, it can terminate the lease within sixty days. Eastern may assign its lease to a successor or subsidiary company, without prior approval.

South Terminal Corporation has a substantially similar clause which also permits assignment and subletting with the Authority's approval. This clause also directs the Authority to terminate its lease with any carrier member of the corporation which breaches either the Massport lease or the South Terminal Interline Agreement (Massport must determine whether such a breach has, indeed, been committed). In the event of such a termination, Massport may then assign or sublet the terminal space to another carrier, which will become a member of South Terminal Corporation at that time. The Interline Agreement further states that the Corporation may choose to sublet vacated space, itself, or assign the space to Massport to lease. South Terminal also has the right to enter into handling agreements with other carriers, whereby a carrier may allow a new entrant to use its facilities and will provide services for the new entrant, but the original carrier will retain the leasehold of the space.

The new Northwest lease devotes a great deal of space to assignment, subletting, and gate utilization/recovery clauses. There is an emphasis on the issue, of gate recapture at Logan, and Northwest's is the first lease in which such provisions have been successfully negotiated.

The lease grants Northwest preferential use of six gates in Volpe Terminal for domestic operations. The current tenants at these gates: NY Air, Pan American, and Continental, will move to South Terminal as subtenants of Massport, which will act as a subtenant of Northwest. The remaining gates in the terminal are used for international operations.. The latter are Massport-controlled (the only such gates on the airport), and are designated for common use by international flights. The term "preferential use" is defined as follows:

> Scheduling preference shall be accorded only to those operations (arrivals and departures) which occur pursuant to a schedule published in the Official Airline Guide.... Airline's charter or extra section operations and/or flights delayed outside of the use period defined herein, shall be accorded preference over like operations by another carrier, but not over the then existing scheduled operations by another air carrier on Airline's preferential gates.(Northwest lease, p. 3)

Northwest is allowed use of its preferential gates for scheduled operations for periods of:

(1) thirty minutes prior to and after a scheduled departure of a turnaround flight (This stipulation is somewhat surprising because it allows an aircraft only one half-hour to arrive and completely board a turnaround flight. Northwest will have to operate very efficiently in order to meet its own departure schedule, and this provision of the lease may force many of Northwest's flights to depart late. Massport insisted upon limiting gate time for turnaround flights to one hour, however, and it was Northwest which chose the thirty-minute/thirty-minute split);

(2) sixty minutes prior to a scheduled departure of an originating flight;

(3) thirty minutes prior to and sixty minutes after the scheduled arrival of terminating flight--if passengers are actively deplaning sixty minutes after arrival, the time allowed can be extended.

The Authority will have the right to schedule operations by other carriers at all other times, upon reasonable notice to Northwest. The airline may use its own discretion in making equipment or personnel available to other carriers, and it may impose reasonable charges for use of its facilities.

This section goes on to acknowledge:

> Airline and Authority recognize the need to maximize the efficient use of all gates at the Airport, and will use flexibility in employing the defined time periods in order to achieve this efficiency requirement, particularly in the event of wide spread delays attributable to air traffic control, weather or similar causes. The Authority recognizes Airline's need to maintain its own schedule and will work with local Airline management to avoid gate scheduling practices which undermine the on-time performance of the Airline. Should the scheduling by the Authority of any individual flight conducted by carriers, other than Airline, on any of Airline's preferential gates result in the disruption of any scheduled flight of Airline three times during any thirty day period, Authority shall be required to reschedule the other carrier's gate use to eliminate the problem.(Northwest lease, p. 4; emphasis in text)

The lease then goes on to define the method for determining acceptable levels of utilization of gates. Massport may evaluate utilization based upon passengers per gate for the preceding twelve months, operations per gate for the preceding twelve months , average aircraft ground time (excluding overnight) and other such indices. Activities of subtenant airlines are included in these evaluations unless jetway structured gate positions are used for ramp loading operations (as might be the case with a commuter subtenant).

The carrier's utilization rate is then compared with that of other airport lessees. Airport lessees are defined as those who have entered into agreements with gate scheduling/recapture clauses (Northwest is the only such carrier at this time), or those carriers which are subject to termination by Massport upon thirty days' notice (e.g. Delta). If the carrier receives a low utilization designation and is among the three lowest utilizers among airport lessees, Massport may require that the carrier accommodate a new entrant carrier which

has been unable to successfully negotiate for terminal space on its own.

Northwest may enter into either a sublease or handling agreement with the new entrant. This agreement must be for a term of at least one year and is not cancelable by the carrier unless the new entrant defaults or the Authority finds less utilized space with which to accommodate the new entrant. Northwest may charge the new entrant based only upon directly related capital and operating costs for its services or facilities.

The Northwest lease also includes a clause entitled "Change of Gate Status". If the carrier fails to accommodate a new entrant carrier according to the above provisions, Massport may convert an airline preferential gate to an "Authority Gate":

> An Authority gate shall be scheduled and controlled by the Authority except that Airline shall retain the right to schedule its "Base Peak" level of flights on that gate. The term "Base Peak: shall mean the maximum number of times per day that Airline simultaneously occupies, in accordance with the Official Airline Guide schedule, all of its preferential gates at any time during the six months immediately preceding the conversion. (Northwest lease, p. 10)

For example, if, during a six month period, Northwest occupies all six of its gates (with flights that are <u>on schedule</u>) at three different periods during one day, these three periods will be considered the base peak. If the schedules change and, at some point, all gates are occupied at four different periods in one day, the four periods will become the base peak--four in one day being the maximum number of such periods that have been observed during the six months.

The "Change of Gate Status" clause continues:

> If, after a period of one year following conversion to an Authority gate, Airline continues to have a lower utilization rate on the Authority gate than other airlines using the gate, then Authority may designate said gate as a

> Common Use Gate that will be subject to the Authority's Common Use provisions. (Northwest lease, p. 11)

The wording of the gate utilization/recapture clauses in the Northwest lease reflects several concerns of the airport administration. For instance, the "Base Peak" concept arose out of a desire to support and encourage international flights.[12] Massport does have an interest in Logan being an international airport, and recognizes that Northwest's international operation will require that domestic flights be able to make connections with international departures. International departures tend to be bunched together because of a desire to land abroad within particular time windows. Thus, in order for a domestic-to-international operations to work well, several gates will be simultaneously occupied at particular times of the day. This is the Base Peak.

The Northwest gate utilization clauses are also written with subleases in mind. Subleasing is rewarded by the fact that sublease arrangements push up utilization rates. There is, therefore, an incentive to sublet space. The requirement that subleases and handling arrangement charges be in line with actual costs arises out of a desire to prevent holding gates idle--which sometimes happens as a result of "gate profiteering". Gate exchanges at the busiest U.S. airports have been known to cost as much as four million dollars.[13] Assignment and sublease clauses grant the airport the right to disapprove gate exchanges, but also state that approval shall not be "unreasonably" withheld. This stipulation can prevent these clauses from being used to stop gate profiteering. Some carriers do appear to be "banking" surplus gate space at some airports. Obviously, this practice lowers an airport's overall level of utilization of gates. The practice of charging a high fee for a sublease or transfer of gates can also cause some carriers to be financially unable to enter a market.

The gate-use clauses in the Northwest lease are a well thought out beginning toward anticipating some of the problems Logan may be facing in the future, regarding it's terminal space. This lease only covers six gates within one terminal, however, and cannot encompass all of the complexities involved in the leasing of terminals at Logan. Because of the differences in the various facilities, gate-use clauses at this airport would have to be different for each space. The issues of gate use are also different for each terminal, depending upon the present tenants. For example, in North Terminal, the primary focus would probably be on transferring a gate from one established tenant to another. This is a much simpler process than accommodating a new entrant because it would only involve a gate and not ticket counters, baggage rooms, etc. Also, as mentioned before, some gate-shifting is highly impractical in a setting, such as Logan, with non-contiguous terminals. An airline with its main facilities in one terminal would be seriously affected by being forced to use a gate in another terminal.

In South Terminal gates are exclusively controlled by the leasing carriers, but even if this were not true, problems would exist. An excellent example of such problems can be found in the case of US Air. US Air uses its space in South Terminal at about a sixty to seventy percent utilization rate. One of the reasons they do not sublet any of it is union conflicts. Most of the carriers which would potentially want to sublease the space are non-union carriers. The area, meanwhile, has sixteen gates and one baggage makeup room, with one conveyor belt. US Air union members will not allow any other airlines' employees to take the bags from the conveyor belt.

A preview of the other kinds of difficulties that will be encountered with increased control of gates by Massport occurred when the Authority proposed moving People Express, a "low cost" carrier,

into Northwest's old space in South Terminal. Several airlines complained about the possibility of having the passengers of the low cost carrier mixing with their own passengers at adjacent gates. In a similar vein, Pan American (which has no lease at Logan) complained about being moved into South Terminal from Volpe Terminal because it was considered a loss of a marketing advantage for an international airline to be moved from the international terminal.[14] The carriers, of course, have very real marketing concerns in such situations, and this is an excellent example of how the interests of airports and airlines are sharply diverging.

Because of the wording of the Northwest lease, subleasing will be very important to Northwest in Volpe Terminal, but, again, although for different reasons, the baggage makeup room is the problem. The existing baggage room is inadequate for even one carrier, but there is no room to build another in Volpe. As long as Northwest has a lease Massport cannot take control of the baggage room, even if it recaptures control of gates for reason of underutilization. This lack of adequate baggage rooms limits the Authority's ability to make the most efficient use of the rest of the terminal space, all the more so because Nothwest holds a lease for the baggage room. Facillities such as baggage rooms are not visible to the public, but can impose constraints which are just as important as those imposed by exclusive gate use.[15]

North Terminal presents yet another difficult and complicated situation. Despite the fact that the carriers in this building have no leases, their gates are not authority controlled. This is because the carriers own all of the loading bridges, which, practically speaking, constitutes control over gates. In theory, these unleased gates could be authority controlled. Massport would simply have to buy its own loading bridges, and order the carriers to move theirs out.[16] If the

carriers chose to fight such a move, however, despite the absence of leases, Massport's only option would be to take the fight to the courts of law. This can often be time-consuming and ineffective. The Authority's flexibility and power to act quickly is, therefore, impaired.

The particular problems faced by officials at Logan in assuring efficient utilization and access to new carriers, then, are complex. They grow out of the design of the airport, the environmental constraints upon the airport, leases which were written for another era, and the demands of the airlines, which sometimes conflict with all of the above.

Termination Clauses

A final point for consideration is the circumstances under which termination of leases can take effect. These clauses, in all three leases are not remarkable or unusual. Briefly, the Eastern lease grants Massport the right to terminate if:

(1) the airline files a voluntary petition in bankruptcy or a court takes jurisdiction over its assets;

(2) the airline defaults in any of the terms and covenants of the lease.

Eastern may terminate the agreement if Massport defaults upon any terms or covenants of the lease.

Massport, along with many other airport operators, is concerned about the effectiveness of its bankruptcy clause. At one time, the Authority attempted to negotiate with Eastern to buy back the lease, in order to assure that it would not lose control over the space to a bankruptcy court. The negotiations, however, came to nothing.

In the case of the South Terminal Corporation lease, Massport may terminate if

(1) the corporation files for bankruptcy or such proceedings are instituted against it;

(2) South Terminal Corporation defaults upon any of the terms of the lease.

South Terminal Corporation may terminate if Massport defaults upon any of the terms of the lease.

At first, it appears that bankruptcy is not an issue in this terminal because the corporation will not go bankrupt unless all of the carriers involved go bankrupt at once. However, a carrier's bankruptcy does represent a default of the Interline Agreement. In this case, the space of an individual carrier could still be tied up by the bankruptcy courts. Massport, rather than the terminal corporation would bear the burden of of vacant space in such an event, because the corporation is not required to be responsible for vacant space.

The Northwest lease may be terminated by Massport if:

(1) the airline defaults upon the terms of the lease;

(2) the airline abandons scheduled service to the airport for sixty days;

(3) a court prohibits the carrier from providing scheduled service at the airport for sixty days;

(4) the carrier's certificate to operate is suspended or terminated for sixty days or more;

(5) the carrier violates any provision of the non-discrimination and affirmative action clause of the lease.

Northwest may terminate if:

(1) the airport is closed to all scheduled air transportation services for sixty days or more;

(2) the Authority defaults upon the terms of the lease.

A bankruptcy clause is noticeably absent in this lease. The gates, of course, are not leased exclusively to Northwest, but only preferentially. Such an arrangement, then, may serve to prevent airport gates from being controlled by the courts as well as preventing their being controlled by the airlines.

The other issues that arise when termination by airlines is considered are not matters of great concern at Logan. Unlike Atlanta, Boston is not dominated by one or two carriers which would leave it more than half empty if they departed from the market. Massport also need not worry about losing revenue. Ninety percent of its passengers are originating or terminating in Boston, and some carrier will serve those passengers no matter what happens. Aside from the uncertainties of a carrier's bankruptcy, then, termination clauses claim very little of the aviation department's attention.

Conclusion

There is now a study being conducted of whether expansion of the Volpe Terminal is needed. The fact that the Eastern lease expires in 1992 could be important to this study if it were known that those gates would come under Authority control, but no such plans for that terminal have actually been formulated. The fact that most of the other gates are not authority controlled, of course, also has an impact on the airport's gate needs.

Volpe Terminal expansion is being considered because problems of where to put the carriers are constant at Logan, and because forecasts indicate that passenger traffic will continue to grow. This is partly because of capacity constraints,but also because of facilities which

are inappropriate. Volpe is not well designed for domestic services (and most of the passenger growth at Logan has been domestic), and commuters really have no appropriate terminal space on the airport. The non-contiguous terminals, of course, also are an issue. Building onto Volpe Terminal may not be the answer for most airlines already at the airport, but according the airport master plan done in the late 1970's, Volpe is the only place to add more gates a significant number of gates.[17] The pproblem may not really be a need for more gates, but a need for more gates where there can be none built.

Logan is very different from the other airports in this study in waya other than those already mentioned. It is highly likely to face severe capacity problems in the next decade, and it cannot significantly expand either its airfield or its terminal capacity. (The airport is already approaching capacity levels in its ground access facilities, but this is outside of the scope of this study.) In addition, Logan's physical layout grew and developed without any overview of the airport as a functioning whole.

The question of whether any exclusive leases at all make sense for Logan has not really been addressed. The carriers who rent on a monthly basis do so more as a matter of accident than a matter of policy. A clear policy stand was taken on gate utilization and control, but when this resulted in no leases with several major airlines, the issue of actively forming a new type of relationship with these carriers was never addressed. As a result, the carriers control their space as if it were exclusively leased.

As a result, Logan's leases, like its terminals are non-uniform and written to address the situation of the moment. In many ways, this is the only sensible way to address the needs of such varied

facilities. Unfortunately, the policy regarding leases is equally non-uniform, and does not include an overview of the directions in which the airport should go.

# CHAPTER SEVEN: CONCLUSION

Charles Barclay, Executive Vice President of the American Association of Airport Executives, commenting on changes in airport administration since deregulation observed, "Airport managers in the past kept the grass mowed and the lights lit, and negotiated with the airlines every thirty years."[1] While the job of airport management has actually required a bit more than this, it is true that the task was less complicated in the past than now years. One of the primary reasons for this is that once terminal and apron space was leased to the airlines, they took primary responsibility for managing it.

The philosophy that airlines should be involved in airport decisions in a major way has been a prevalent one from the beginning of commercial aviation in this country. Airlines, after all, pay user fees to airports, and are deemed to be in a better position to determine what facilities can most efficiently promote air travel. Two assumptions have supported this position throughout the years:

(1) Airports exist primarily to serve and promote air transportation. Therefore, their first responsibility is to the travelling public, and, indirectly, to the airlines because serving the airlines well promotes better service to the travelling public.

(2) The airlines know how to best manage an air transport system, and as profit-making entities, are in a better position to take the financial risks involved in providing airport facilities.

This is an attitude that is beginning to change as many airport administrators are attempting to solve problems that affect the entire airport system, e.g. airfield or terminal congestion. It is becoming

as made:

> The need for an assumed supply of resources makes it attractive and sometimes imperative to establish formal relationships between organizations. Pooling of resources toward common objectives in joint programs is one method of enhancing the resources of an organization, but management is faced with a difficult dilemma. The resource benefits of association are coupled with the potential detrimental effects of bringing members of the other organization, whose objectives and priorities are not necessarily equivalent or compatible, into the operation of the joint program and, therefore, into the decision-making structure of the focal organization. The more influential the outside organization becomes in this way, the more likely that the character of the home organization and the integrity of its priorities will be altered....The dilemma, then, is whether to acquire the benefits of joint action and risk dilution of organizational objectives, or to forgo the benefits of a relationship and maintain the autonomy of the separate priorities.[2]

It is on the horns of that dilemma that airport administrators are perched today. For some airports, a crisis point will be reached in the next decade. This crisis is currently being precipitated by continually growing passenger demand which will lead to severe capacity problems, and by the environmental pressures which will prevent airports from expanding.

Deregulation is additionally affecting this situation by allowing air carriers to enter and exit markets at their own discretion. Some airports in the U.S. have experienced periods of phenomenal growth at various periods in the past seven years as deregulation has allowed the carriers to restructure their route systems around major hubs. Kansas City International's growth of the past two years is one such example.

Airline deregulation has other implications for airports, however, which have not been as visible. The administrators of the airports included in this study have all cited as a major concern the accessibility of the airport to new entrants. Before deregulation, such issues were the responsibility of the CAB. Now, however, some aspects of assuring free competition have fallen to the airports. Airport administrators, then, must balance the demands of free competition in the industry, the operating requirements of the carriers, the balance of the environment, and the air transportation needs of the community. In order to do this, airport operators must have the power to set priorities without undue influence from any one group over another, and the flexibility to act as they see fit.

The price that will have to be paid for such power and flexibility is that airports will have to somehow assume the financial risk for their own development. The airlines, understandably, will no longer be willing to take these risks if their own priorities are not to be foremost in the minds of airport administrators. Airports, then, will no longer be joint enterprises between airport administrators and airlines.

The three airports presented here are probably not different from any other airport in the United States in that they find themselves at the crossroads between the practices which once were adequate and the realization that these practices are adequate no longer. In examining the leases, it can be seen that changes have been instituted, but that they are, for the most part, limited changes. None of the three airports is contemplating a major overhaul of its leasing policies, and all of the changes which have been made are very much within the context of the airports' immediate situations.

Atlanta-Hartsfield has just made a major investment in a large brand-new terminal facility. The new terminal was badly needed, is well-designed for Atlanta's traffic, and represents good planning. The need to build and finance it, however, has caused all other concerns to take a secondary position. Given the options available for capital financing of airports, especially for a market with sixty-five to seventy-five percent transfers, Atlanta chose the traditional route of long-term, exclusive leases, MII clauses, and guarantees that the terminal investment will be amortized by airline use fees.

Kansas City International represents an entirely different situation. With no plans for expansion in the near future, and no ambitions to become an overly large hub, the airport is far less dependent on its airlines than Hartsfield. Currently, KCI's future looks bright because of Eastern's hubbing effort, and because KCI is an attractive alternative to the highly congested Midwestern hubs in Chicago and Denver. By recognizing the need for strong, active airport management, the Aviation Department can plan ahead to avoid some of the undesirable developments it sees taking place at other airports. Some of the lease provisions which already exist indicate such a tendency on the part of airport administrators. Again, however, the airport's response is partly dictated by the situation of the moment. Because there is no immediate need for airport management to take firm control over terminal space, the gate use and recapture clauses, for example, do not impose stringent requirements. KCI's ability to respond before a situation reaches crisis levels may be crucial to its future. That ability has yet to be tested.

Boston-Logan, of the three airports, is the one faced with the most imminent problems. Again, it has addressed itself only to immediate issues. The Northwest lease contains strong provisions for

gate recapture by the airport, on the one hand, and, on the other, possibly constrains the airport because of its twenty-five year term. The other long-term leases are the result of older practices, and little can be done about the terminals which they cover until the leases expire. The terminals which are not covered by leases, however, are an obvious place to institute stronger airport control, but because there is no immediate requirement for such action, none has been taken. No policy has been formulated for these areas of the airport at all.

In 1981, John Wiley, former Director of Aviation for the Port Authority of New York and New Jersey, wrote:

> airports must be considered as parts of the total social, economic and political systems in which they exist and not be relegated narrowly to aviation issues nor even to the wider, but still incomplete systems defined by transportation issues. The mandate to the airport administrator is clear—participate in the broadest applicable system planning concept....[3]

Consistent with this line of thinking, the wave of the future seems to be one of increasing differentiation between airports and airlines. Upon reflection this makes sense. Aviation has traveled far beyond the days of visions of unlimited growth, when airports and airlines had a similar purpose and similar goals: to further this growth together. The pressures that airlines experience are just as serious as those of airports, but of a very different nature. Airports do not fly away like the aircraft that use them. They are permanent parts of the communities in which they reside, and the decisions made by airport managements have economic, environmental, and political implications for these communities.

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# APPENDICES

HARTSFIELD ATLANTA AIRPORT USE AGREEMENT (excerpts)..................154

CITY OF ATLANTA: AGREEMENT AND LEASE, CENTRAL PASSENGER
TERMINAL COMPLEX (excerpts)..........................................156

KANSAS CITY INTERNATIONAL AIRPORT, USE AND LEASE
AGREEMENT (excerpts).................................................158

KANSAS CITY INTERNATIONAL AIRPORT USE AGREEMENT (excerpts)..........163

AGREEMENT BETWEEN MASSACHUSETTS PORT AUTHORITY (ADMINISTERING
LOGAN INTERNATIONAL AIRPORT, BOSTON) AND EASTERN AIRLINES
(excerpts)...........................................................164

LOGAN INTERNATIONAL AIRPORT, BOSTON, AGREEMENT FOR THE
CONSTRUCTION AND LEASING OF THE SOUTH TERMINAL, MASSACHUSETTS
PORT AUTHORITY AND SOUTH THERMINAL CORPORATION, et al.
(excerpts of Guaranty and Indemnification Agreement of
AMERICAN AIRLINES)...................................................166

LOGAN INTERNATIONAL AIRPORT, BOSTON, MASSACHUSETTS PORT
AUTHORITY, TERMINAL E, BOSTON-LOGAN INTERNATIONAL AIRPORT,
LEASE AND AGREEMENT WITH NORTHWEST AIRLINES, INC. (excerpts).....168

# HARTSFIELD ATLANTA AIRPORT
# USE AGREEMENT
# (excerpts)

## II. TERM

The rights and privileges granted under this instrument shall extend for a term beginning on the 1st day of July, 1982, and ending on the 21st day of September, 2010.

## VI. BASIC LANDING FEE

The Airline shall pay to the City each month a Basic Landing Fee computed at the rate of Sixteen Cents per 1,000 pounds of the Federal Aviation Administration Maximum Certificated Gross Landing Weight of each aircraft scheduled to land at the Airport during such month as shown in the timetables of the Airline on file with the Civil Aeronautics Board (or its successor agency) as of the first day of such month.

## VII. FIELD IMPROVEMENTS LANDING FEES

With respect to the major airfield improvements which the City undertook with the approval of a Majority In Interest of the Atlanta Airlines and substantially completed under the 1967-72 Airfield Improvements Program, the City issued Airport Revenue Bonds and established a Field Improvements Landing Fee which, from the effective date of this Amendment No. 6, shall be known as the annual Initial Field Improvements Landing Fee. The Airline agrees to pay its proportionate share of the annual Initial Field Improvements Landing Fee.

...

With respect to other major airfield improvements (including acquisition of land and site preparation thereof for a second air carrier airport for the Atlanta area), for which annual Additional Field Improvements Landing Fees are required, the City shall submit to the Atlanta Airlines a summary of each proposed airfield improvement and justification therefor and, if a Majority In Interest of the Atlanta Airlines approve the proposed improvement, the City will then undertake to diligently accomplish said improvement in accordance with said proposal and all terms, conditions, and provisions attendant thereto. The Airline agrees to pay its proportionate share of the City's costs of such approved improvement in the form of an annual Additional Field Improvements Landing Fee.

## VIII. LAND RENTALS

Should the City lease any ... property to a party other than one of the Atlanta Airlines, the annual land rental charged shall be not less than the amount which would be charged an Atlanta Airline.

Any and all net rentals received by the City from such properties shall be credited against the Field Improvements Landing Fee payable by the Atlanta Airlines under the provisions of Article VII of this Agreement.

## XVII. TERMINATION BY CITY

The City, in addition to any right of termination or any other right herein granted to it, or accruing to it by operation of law, may declare this Agreement terminated in its entirety upon the happening of any one or more of the following events . . .:

1. If the rentals, fees, charges, or other money payments which the Airline herein agrees to pay, or any part thereof, shall be unpaid on the date the same shall become due, or
2. If the Airline shall file a voluntary petition in bankruptcy, or make a general assignment for the benefit of creditors, or
3. If any act occurs which operates to deprive the Airline permanently of the rights, power and privileges necessary for the proper conduct and operation of its business, or
4. If the Airline abandons service to the Airport for sixty days or more, except when such abandonment and cessation is due to fire, earthquake, strike, governmental action, default of the City, or any other causes beyond its control, or
5. If any of the covenants or agreements contained herein shall be breached by the Airline.

## XVIII. TERMINATION BY AIRLINE

The Airline, in addition to any right of termination or any other right herein granted to the Airline or accruing to it by operation of law, may terminate this Agreement in its entirety upon or after the happening of any one of the following events:

1. If any act occurs which operates to deprive the Airline of the rights, power and privileges necessary for the proper conduct and operation of its business, or
2. The breach by the City of any of the covenants or agreements herein contained, or
3. The continued failure or refusal by the City after thirty days written notice to the City, to maintain and operate in a reasonably satisfactory manner the public aircraft facilities at the Airport, or
4. The continued operation of the Airport, after thirty days written notice to the City, for the accommodation of types of air traffic other than commercial airline traffic to the extent that use of the Airport by commercial airline traffic is substantially impaired or restricted, or
5. If the Airline abandons service to the Airport for sixty days or more.

# CITY OF ATLANTA: AGREEMENT AND LEASE

# CENTRAL PASSENGER TERMINAL COMPLEX

(excerpts)

## I. DEFINITIONS

1.31 Majority-In-Interest (MII) of the Airlines means fifty-one percent or more of the Contracting Airlines, which have also leased seventy-five percent or more of the total Aircraft Parking and Ramp Area square footage exclusively leased to all Contracting Airlines and seventy-five percent or more of the total Exclusive Leased Premises in the Landside Terminal Buildings and the Concourse Buildings leased to all Contracting Airlines.

## II. TERM AND USE OF PREMISES

2.01 Effective Date and Term. - This Agreement shall become effective upon execution and delivery by City and Airline and shall continue in effect during the lease term. The lease term shall commence as of the DBO ["Date of Beneficial Occupancy" of the CPTC], but in no event later than January 1, 1984, and shall continue for thirty years thereafter.

## IV. LEASED PREMISES

4.06 Subletting of Leased Premises. - Airline may sublet its Leased Premises, in whole, or in part, to any other air carrier, or air carriers, authorized to offer scheduled service at the Airport; provided, that unless the City consents in writing to release Airline therefrom, which consent shall not be unreasonably withheld, no such sublease shall serve to release Airline from any of its obligations, duties or responsibilities with respect to such Leased Premises under this Agreement, and provided, further, that no such subletting shall be at a rental charge in excess of that charged to Airline by the City under this Agreement, plus the unamortized investment of Airline in improvements, fixtures, and equipment installed by it at its expense, unless such excess be assigned to the City as additional rental under this Agreement, and provided, further, that any subletting shall be subject to termination by the City in the event that the sublessee's authority to offer scheduled service at the Airport is rescinded, revoked, or otherwise terminated.

9.17 Events of Default By Airline. - Each of the following shall constitute an "event of default by Airline":

(A) Airline shall fail to make due and punctual payment of the rentals and charges payable hereunder, and such default shall continue for a period of fifteen days after receipt of written notice from City of such non-payment.

(B) Airline shall fail after the receipt of thirty days written notice from City to keep, perform or observe any other material term, covenant or condition of this Agreement....

(C) Airline shall file a voluntary petition in bankruptcy, or make assignment of all or substantially all of Airline's assets for the benefit of Airline's creditors, or Airline is adjudicated a bankrupt in any involuntary proceeding in bankruptcy against Airline, or a receiver of the assets of Airline, is appointed; provided, however, that in the latter event if any such appointment is involuntary, then it shall not be considered an event of default by Airline unless Airline fails to procure a dismissal thereof within sixty days after the appointment of such receiver.

## IX. PROVISIONS OF GENERAL APPLICATION

9.18 Remedies for Airline's Default. - Upon the occurrence of an "event of default by Airline", City, besides any other rights or remedies it may have, shall have the immediate right of re-entry and may remove all persons and property from the Leased Premises.... No such reentry or taking possession of the Leased Premises...by City shall be construed as an election on its part to terminate this Agreement unless a written notice of such intention be given to Airline.

9.19 Events of Default by City. - Each of the following events shall constitute an "event of default by City":

(A) City shall fail after receipt of thirty days written notice from Airline to keep, perform or observe any material term, covenant or condition of this Agreement to be kept, performed or observed by City.

(B) City shall close the Airport to flying in general or to the flights of Airline, for reason other than weather, acts of God or other reasons beyond its control, and fail to reopen the Airport to such flying or flight for a period in excess of ten days.

(C) City shall deprive Airline of its right to occupy and use the Leased Premises in accordance with the terms of this Agreement for a period in excess of ten days or deprive Airline of its right to use the Airport in accordance with the terms of the Airport Use Agreement, as it may be amended from time to time, for a period in excess of ten days.

9.20 Remedies for City's Default. - After the occurrence of an "event of default by City" Airline shall have the right to terminate this Agreement upon thirty days written notice to City....

9.21 Airline's Right of Termination. - Airline, in addition to any other right of termination provided for elsewhere herein or by operation of law, may terminate this Agreement upon ten days written notice to City after the happening of any of the following events:

(A) The Airline shall be permanently deprived, for any reason beyond its control, of the rights, certificates, or authorizations necessary under applicable law to operate its air transportation business at the Airport.

(B) The Airport shall be closed, on a permanent basis, to flying in general or to the flights of Airline, for any reason beyond Airline's control.

9.26 Assignment or Transfer. - Airline shall not sell, assign or transfer this Agreement without the prior written consent of City; provided, however, this Agreement may be assigned by Airline without such consent to any successors-in-interest of Airline with or into which Airline may merge or consolidate which may succeed to the assets of Airline or a major portion thereof related to its air transportation business.

# KANSAS CITY INTERNATIONAL AIRPORT

# USE AND LEASE AGREEMENT

(excerpts)

## ARTICLE I
## DEFINITIONS

F. "Majority in Interest" means, unless otherwise indicated in this Agreement, those scheduled airlines (but in no event less than one-third of the number of airline parties to this Agreement) having, on the date in question, more than fifty percent (50%) of the total revenue aircraft weight landed at the Airport during the six (6) calendar months preceding the month in which the date in question occurs.

## ARTICLE II
## LEASED PROPERTY

Section 203. Aircraft Loading Apron....When Airline has no aircraft requiring use of the apron loading position, the City may allow others to use the apron as circumstances and the public interest require. Airline agrees to minimize its time of usage of the aircraft loading apron and to remove its aircraft promptly when they are not being loaded or unloaded if the City notifies it that one or more of its aircraft loading apron parking positions is required for use by others. Whenever Airline is required to remove its aircraft from the aircraft loading apron pursuant hereto, the City shall provide paved aircraft parking space in an area supported by landing fees. Where practicable, Airline shall not be required to accommodate another carrier offering directly competing service in markets served by Airline.

Use of the apron area by aircraft of others than Airline may require access to Airline rented hold-rooms adjacent to the loading apron area and may even require, if Airline gives its permission, the use of Airline-owned and installed airplane loading devices. If such use is to be made of Airline rented apron and/or hold-room and/or Airline-owned airplane loading devices, Airline shall be properly compensated for such use by the user of the facilities. Such compensation shall not exceed Airline's pro rata direct costs plus a reasonable administrative charge. It is expected that this would be accomplished by an agreement mutually satisfactory to Airline and the aircraft operator requiring the use of the facilities. If the carrier being accommodated requires ground handling of its aircraft and/or processing of its passengers and their baggage, it shall have the right to contract with Airline or any other party for such services

and shall not be required to secure such services from Airline as a condition of using Airline's facilities. If a mutually acceptable method and amount of compensation for such use cannot be agreed upon between Airline and the aircraft operator requiring secondary use, then City reserves the right to determine what a fair and proper compensation method and amount should be and impose it on the parties.

Section 206. Level of Service. Notwithstanding the rights granted by any other provision hereof, including the right to quiet enjoyment of the exclusive and preferential use premises leased hereunder, Airline's continuing right to use and occupy any aircraft loading apron position and its associated ticketing, hold-room and baggage handling space (defined for purposes of this section as a "gate position") is contingent on Airline maintaining a specified level of activity in such facilities. Any gate position shall be deemed underutilized if the average weekday flights of Airline's aircraft arriving at that gate position is 35% less than the then current average gate utilization of all scheduled air carriers operating aircraft of a similar size and having similar agreements hereto with the City.

If, at any time, one or more of Airline's gate positions is underutilized, and remains so for a period of six months, and any other scheduled air carrier expresses its willingness to utilize the gate(s) at a higher level than the current average utilization of all scheduled air carriers operating aircraft of a similar size, then that carrier shall have the right to acquire Airline's improvements in the gate position(s) and enter into an agreement similar hereto for the use and occupancy of the premises as a substitute for Airline. Airline shall have the right to receive, as compensation for the acquisition of its improvements, the unamortized value thereof and shall not be obligated to sell any of its trade fixtures. If Airline and the other carrier are unable to agree upon a price for the improvements within sixty (60) days after notice from the City that the other carrier intends to acquire the gate position(s), then the price shall be established by arbitration.

## ARTICLE III
## LEASE TERM

Section 301. Term. The term of this Agreement, and the payment of rental, use-fees and advances hereunder, shall commence on February 1, 1984 and shall expire on May 31, 1998.

## ARTICLE IV
## RENTAL AND USE-FEES

Section 403. Field and Runway Use-Fees. Airline hereby agrees to pay compensatory fees to the City for Airline's use of the field and runway area until [date], the use-fee rate at the Airport shall

be 67.68 cents per thousand pounds for Airline's aircraft landed on the Airport in revenue flights.

Annually on May 1st, use-fee rates shall be revised and adjusted to provide that City's total revenue from the field and runway area shall be equal to the City's expense of the field and runway area.

Section 407. Annual Re-Calculation of Compensatory Rentals and Use-Fees. Compensatory rental rates and field and runway use-fees shall be computed by determining the expense to the City of interest on the City's investment in land and interest and depreciation on City's investment in facilities at the Airport exclusive of Federal and/or State grants-in-aid. Said investment shall include appropriate distribution of the cost of systems and site improvements. To this annual interest and depreciation expense there shall be added the City's expense of maintenance and operation of the demised premises and/or the field and runway area as the case may be, and the appropriate distributable share of the City's maintenance and operation expense of the Airport systems and mechanical areas. Examples of such systems are: water, sanitary and storm sewers, electrical and communications, heating and air conditioning, fire protection and service roads.

When capital improvements to the field and runway area, with the exception of the purchase of land and those improvements planned as initial construction, become necessary or desirable, the City and the scheduled airlines serving the Airport including Airline agree to discuss such proposed improvements in an effort to arrive at a mutually satisfactory agreement with respect to physical plans and changes or adjustments in use-fees or rentals. In the absence of such mutually satisfactory agreement between the City and the majority in interest of the scheduled airlines, the City shall not be obligated to make said capital improvements but, if it proceeds with the improvements without the consent of the majority in interest of the scheduled airlines, the cost of such improvements shall not be taken into consideration in determining said use-fees and/or rentals.

## ARTICLE VII
## ASSIGNMENT AND SUBLETTING

Section 701. Assignment and Subletting. Airline agrees not to assign this Agreement or any part thereof in any manner whatsoever or to sublet the premises or any part thereof or any of the privileges recited herein without the prior written consent of the Director. Airline shall have the right to assign all or any part of its rights and interests under this Agreement to any successor to its business through merger, consolidation or reorganization or voluntary sale or transfer of substantially all of its assets, and the consent of the City thereto shall not be required, but due notice of any such assignment shall be given to the City within sixty (60) days after such

assignment is executed. In the event of any sublease hereunder, it is understood and agreed that the City does not release Airline from any of its obligations with respect to the terms hereof.

If Airline's sublessee requires ground handling of its aircraft and/or processing of its passengers and their baggage, it shall have the right to contract with Airline or any other party for such services and shall not be required to secure such services from Airline, as a condition of entering into the sublease.

## ARTICLE VIII
## TERMINATION OF LEASE IN ENTIRETY

Section 801. City's Right to Terminate. The City, in addition to any other rights to which it may be entitled by law, acting by and through its Director of Aviation, may declare this Agreement terminated in its entirety, subject to and in the manner provided in Section 803 hereof, upon or after the happening of any one or more of the following events and may exercise all rights of entry and re-entry, with or without process of law, upon the demised premises:

A. The filing by Airline of a voluntary petition in bankruptcy or any assignment for benefit of creditors of all or any part of Airline's assets;

B. The adjudication of Airline as a bankrupt pursuant to any involuntary bankruptcy proceedings;

C. The taking of jurisdiction by a court of competent jurisdiction of Airline or its assets pursuant to proceedings brought under the provisions of any Federal reorganization act;

D. The appointment of a receiver or trustee of Airline's assets by a court of competent jurisdiction or a voluntary agreement with Airline's creditors;

E. The voluntary abandonment by Airline or the conduct of its air transportation business at the Airport; or

F. The breach by Airline of any of the covenants or agreements herein contained and the failure of Airline to remedy such breach.

Section 802. Airline's Right to Terminate. Airline, in addition to any other right given to it herein, may cancel this Agreement in whole or only insofar as it relates to any building, and terminate all or any of its obligations hereunder at any time, upon or after the happening of any one of the following events:

A. The issuance by any court of competent jurisdiction of any injunction in any way preventing or restraining the use of said Airport or of any part thereof for airport purposes and the remaining in force of such injunction for a period of at least sixty (60) days;

B. The breach by the City of any of the covenants or agreements herein contained and the failure of the City to remedy such breach;

C. The inability of Airline to use said demised premises and Airport facilities for a longer period than ninety (90) days due to war, earthquake or other casualty;

D. The erection of any obstacle on or in the vicinity of said Airport which would occasion a modification of Airline's air carrier operating certificate or similar authorizations establishing minimum safety standards for the operations of Airline;

E. Any action of any governmental authority, board, agency or officer having jurisdiction thereof preventing Airline from conducting its air transport business at the Airport by the taking, directly or indirectly, in whole or a substantial part, of the demised premises or premises required for actual operation of Airline's aircraft to and from the Airport;

F. The taking through the process of eminent domain of all or a substantial part of the premises and space leased by Airline; or

G. The termination or suspension for more than inety (90) days by any governmental authority, board, agency or officer having jurisdiction of Airline's certificate of public convenience and necessity authorizing it to serve Kansas City, Missouri.

Airline shall not exercise any cancellation right set forth above unless, prior to such cancellation, the City has in hand contracts and leases of equal value to those Airline seeks to cancel from another scheduled airline or from the remaining scheduled airline tenants at the Airport, but this limitation on cancellation shall apply only so long as Kansas City General Improvement Airport Revenue Bonds, Series September 1, 1967, shall be outstanding.

# KANSAS CITY INTERNATIONAL AIRPORT

## USE AGREEMENT

(excerpts)

(2) Term. Except as hereinafter provided, the term of this Agreement shall begin November 1, 1984 and shall end on October 31, 1985.

(3) Termination. The City reserves the right to terminate this Agreement if the Airline violates any of the terms hereof. Such termination shall become effective immediately after the Director of Aviation shall have given written notice of such violation to the Airline.

(4) Landing Fee. The Airline agrees to pay to the City a fee of Sixty-Four Cents ($0.64) per thousand pounds of aircraft landed weight landed at the Airport. The $0.64 per thousand pounds rate is the currently applicable rate payable by our tenant certificated air carriers plus 15% and is the same as that charged to all non-tenant certificated air carriers at the Airport. The landing weight of aircraft to be reported and paid on is the FAA maximum approved landing weight of aircraft at the Airport. The City reserves the right to change the above-stated landing fees by the Director of Aviation giving thirty (30) days written notice to the Airline.

# AGREEMENT

# BETWEEN

# MASSACHUSETTS PORT AUTHORITY

# (ADMINISTERING LOGAN INTERNATIONAL AIRPORT, BOSTON)

# AND EASTERN AIRLINES

(excerpts)

## ARTICLE II
## LEASE

1. <u>Term</u>

Effective on the Completion Date hereinafter defined, Authority demises and lets unto Airline and Airline hires and takes from Authority all of Tract "A", Tract "B" and the Terminal Facility then constructed thereon (collectively the "demised premises") for the uses hereinafter set forth, for a term of twenty-five (25) years from the Completion Date,...

## ARTICLE VII
## Termination

1. <u>Termination by Authority</u>

In the event that Airline shall file a voluntary petition in bankruptcy or that proceedings in bankruptcy shall be instituted against it and not dismissed within thirty (30) days, or that a court shall take jurisdiction of Airline and its assets pursuant to proceedings brought under the provisions of any Federal reorganization act, or that a receiver of Airline's assets shall be appointed and such taking or appointment shall not be stayed or vacated within a period of sixty (60) days, Authority may thereupon terminate this Agreement by fifteen (15) days' prior written notice to Airline. In addition, of Airline shall fail to perform, keep and observe any of the term,s covenants or conditions herein continued on the part of Airline to be performed, kept or observed, [Authority may terminate this agreement].

3. <u>Termination by Airline</u>

If Authority shall fail to perform, keep and observe any of the terms, covenants or conditions herein contained on the part of Authority to be performed, kept or observed, Airline may give Authority notice in writing to currect such condition or cure such default which notice shall state that it intends to terminate this Agreement

if Authority fails to carry out its obligations with respect to correction or cure....

## ARTICLE VIII
## Assignment and Subletting

Airline shall not assign or transfer this Agreement without the prior written approval of the Authority except that no such approval shall be necessary if the assignee or transferee is a successor or subsidiary air transportation company. No such assignment or transfer shall release Airline from its obligation to pay or cause to be paid as and when due the rent specified herein and to perform or cause to be performed its other obligations hereunder or release it from liability for any default of such successor or subsidiary except that if such assignment or transfer is made in connection with the sale of all or substantially all of Airline's assets to a responsible trunk-line passenger aircraft operator which shall assume, by instrument satisfactory to Authority, all of Airline's obligations hereunder, Airline shall have no further obligations hereunder.

Airline shall not sublet any of the demised premises without the prior written approval of the Authority, except:...

(b) Authority will not unreasonably withhold its approval of the sublease of space in or on the demised premises to anyone performing services for Airline in the Terminal Facility for use in connection with such services, and

(c) If Airline's right to serve the Airport for the transportation of persons, property or mail is terminated by legal authority, Airline shall have the right to sublet all or any part of the demised premises without Authority's prior approval provided Airline gives Authority notice of said sublease. If Authority does not approve of such sublease it may, within sixty (60) days of notice of such sublease, terminate this Agreement by notice to !irline in which event if (sic) shall pay Airline the unamortized cost of any leasehold improvements installed on the demised premises by Airline. The amortization period shall not extend beyond the stated term of the lease.

## ARTICLE X
## Miscellaneous

### 2. Additional Charges

...The foregoing provisions of this section shall in no way limit Authority's right to impose nondiscriminatory landing fees in respect to Airline's aircraft or aircraft of Airline's sublessees and suppliers using the Airport.

LOGAN INTERNATIONAL AIRPORT

BOSTON

AGREEMENT FOR THE CONSTRUCTION AND LEASING
OF THE SOUTH TERMINAL

MASSACHUSETTS PORT AUTHORITY

AND

SOUTH TERMINAL CORPORATION, et al.

(Excerpts of Guaranty and Indemnification Agreement of AMERICAN AIRLINES)

ARTICLE II - LEASE

1. Term

The Term of this Lease shall be for a period of Twenty-Five (25) years commencing upon the Completion Date as hereinafter defined in Article II, Section 5, unless sooner terminated as herein provided.

2. Premises

...with the right in the Airlines to use runways, taxiways and aprons to service the Passenger Terminal. The Airlines right to use the runways, taxiways and aprons shall be subject to the Airlines paying uniform landing fees imposed by Authority at rates which shall be generally applicable to all Air Carrier aircraft not paying for any of the above facilities through separate agreements....

19. Assignment, Subletting, License Agreements

Subject to the exceptions noted below, South or Airlines shall not assign this Lease or any part thereof, nor shall South or Airlines sublet the premises or any part thereof, nor shall South or Airlines enter into any license agreements for the premises or the business to be conducted thereon without the prior written approval of the Authority, which written approval shall not be arbitrarily withheld. If any Airline loses its CAB certification to serve Logan Airport,

the Authority will consent to a sublease or assignment of that Airline's portion of the premises to another financially responsible Airline which is certified by the CAB to serve Logan Airport.

In the event that Authority receives written notice from South stating that South wishes to terminate any specific Airline's right to continue to use the Terminal Facilities in conjunction with South for violation of the provisions of this Agreement or the South-Airline Interline Agreement, Authority agrees to execute instruments necessary to evidence termination of this lease as to any specific Airline, provided that the Authority determines that there has been a violation of this Agreement or the Interline Agreement which warrants such a termination.

If there is a termination of any specific Airline's right to use the Terminal Facility in accordance with this Section 19, South shall be relieved of its obligation to pay said Terminated Airline's proportionate share of Base Rent from the effective date of the termination (which date shall not be retroactive)....The Authority shall have the right to assign or sublet that portion of the Terminal Facility previously occupied by said Terminated Airline; provided, however, that as a condition of said assignment or sublease, the Authority shall require (and South shall allow) the assignee or sublessee to become a party to the Interline Agreement....

20. Termination by Authority -

A. In the event that South shall file a voluntary petition in bankruptcy or that proceedings in bankruptcy shall be instituted against it and not dismissed within sixty (60) days, or that a court shall take jurisdiction of South and its assets pursuant to proceedings brought under the provisions of any Federal reorganization act, or that a receiver of South's assets shall be appointed and such taking or appointment shall not be stayed or vacated within a period of sixty (60) days, Authority may thereupon terminate this Agreement by fifteen (15) days' prior written notice to South and Airlines. In addition, if South shall fail to perform, keep, and observe any of the terms, covenants, or conditions herein contained on the part of it to be performed, kept, or observed, other than payment of rent, Authority may give South and Airlines notice in writing to correct such condition or cure such default, which notice shall state that it intends to terminate this Agreement if South fails to carry out its obligations.

22. Termination by South -

If the Authority shall fail to perform, keep, and observe any of the terms, covenants, or conditions herein contained on the part of the Authority to be performed, kept, or observed, South may give Authority notice in writing to correct such condition or cure such default, which notice shall state that it intends to terminate this Agreement if Authority fails to carry out its obligations with respect to correction or cure....

LOGAN INTERNATIONAL AIRPORT

BOSTON

MASSACHUSETTS PORT AUTHORITY

TERMINAL E

BOSTON-LOGAN INTERNATIONAL AIRPORT

LEASE AND AGREEMENT
WITH
NORTHWEST AIRLINES, INC.

(excerpts)

ARTICLE 1 - Term

1.01 This Lease shall be for a term of twenty-five (25) years and shall commence...[OPTION - on the date as set forth in the notice from the Authority that the premises are available to Airline to commence construction of its improvements] and shall terminate on March 31, 2010, unless terminated earlier under any other provision of this Lease.

ARTICLE 2 - Premises

2.03. Use of Gates and Adjacent Apron.

(a) Domestic Operations

Airline shall have preferential use of six gates in Terminal E, counting from existing Gate #3B, southward to existing Gate #1, where Gates #3 and #1 have A and B positions. Airline shall install a "B" position on Gate #2 to embark and disembark passengers.

(b) International Operations

Gates #4 through #8B shall be designated for common use as defined in the Authority's Gate Control and Access Plan (the "Plan") for international operations within the terminal. Airline shall have access to these gates in accordance with the Plan in the same manner as afforded to other carriers designated by the Authority to use said gates in accordance with the Plan. A copy of the Authority's current Plan is attached as Exhibit __. The Authority reserves the right to modify the Plan as it deems appropriate with due consideration for operational, safety and efficiency factors.

(c) Preferential Use

The term "preferential use" as used herein to designate gate utilization rights of Airline shall be construed as follows:

(1) Scheduling preference shall be accorded only to those operations (arrivals and departures) which occur pursuant to a schedule published in the Official Airline Guide (OAG) or any successor publication. Airline's charter or extra section operations and/or flights delayed outside of the use period defined herein, shall be accorded preference over like operations by another carrier, but not over the then existing scheduled operations by another air carrier on Airline's preferential gates. Periodically, the Authority may require for periods of time to be defined at the time of the request, that Airline's schedule changes to be published in the OAG be made available to the Authority at least 45 days prior to the commencement of such operations. Any requested schedule changes not made within the 45 day period shall be scheduled by the Authority in accordance with the Plan.

(2) The period of use by Airline for each such preferential operation shall be as follows:

(i) arrivals and departures of turnaround flights - for aircraft that are scheduled to arrive at Logan and depart directly, the period of use by Airline for gate use scheduling purposes shall commence 30 minutes prior to the time of the scheduled arrival and shall expire 30 minutes after the scheduled departure time. The use period shall terminate upon the actual departure of the aircraft from the gate or thirty minutes after the scheduled departure time, whichever is the earlier to occur. However, the 30 minute limit shall be extended if the aircraft is being boarded and actively preparing for departure, but only to the completion of the boarding process.

(ii) arrival of terminating flights and departure of originating flights - for aircraft with arrivals that terminate at or originate from Logan (such as overnight aircraft or aircraft that have been removed from the gate to accommodate the operations of another carrier), the period of use for scheduling purposes shall commence 60 minutes prior to the time of a scheduled departure and 30 minutes prior to a scheduled arrival. The period of use for a terminating flight shall expire 60 minutes after scheduled arrival or upon the completion of the deboarding process, whichever is the earlier to occur. The period of use for an originating flight shall expire at the scheduled departure time. The 60 minute limit on arrivals shall be extended if the terminating aircraft is actively in the process of deboarding passengers. The departure time shall be extended if the originating aircraft is being boarded and actively preparing for departure. In such instances, the extension shall extend only to the completion of the active boarding or deboarding process.

(iii) The Authority shall upon reasonable notice to the Airline have the right to schedule arrivals and departures by other aircraft operators at all other periods. Examples of the construction of the term "reasonable notice", as used herein, are attached as Exhibit ___. In accommodating the Authority's in its right to schedule operations hereunder, Airline will allow use of its holdroom, baggage claim and such other facilities as may be required for the use of the gate. At Airline's discretion it may make available other equipment and personnel as requested by Authority or air carrier, in conjunction with the use of the gate. Airline at its election may impose on the air carrier(s) using its facilities reasonable charges.

(iv) The time periods defined above represent what the parties believe are reasonable parameters for operational activities at the time of execution of this Lease. Airline and Authority recognize that the Airline's or Airport's operations may require flexibility in the use of these parameters. In addition, Airline and Authority recognize the need to maximize the efficient use of all gates at the Airport, and will use flexibility in employing the defined time periods in order to achieve this efficiency requirement, particularily, in the event of wide spread delays attributable to air traffic control, weather or similar causes. The Authority recognizes Airline's need to maintain its own schedule and will work with local Airline management to avoid gate scheduling practices which undermine the on-time performance of the Airline. Should the scheduling by the Authority of any individual flight conducted by carriers, other than Airline, on any of Airline's preferential gates result in the disruption of any scheduled flight of Airline three times during any thirty day period, Airline shall be required to reschedule the other carrier's gate use to eliminate the problem.

(3) The parties agree to cooperate to ensure that the preferential rights concept set out in this article works effectively. The obligation to cooperate shall include the towing, upon reasonable request, of any aircraft parked at a preferential gate from that gate to an Authority designated aircraft parking position, as adjacent to Terminal E as possible, when the aircraft is not in the period of use as defined above.

Requests for aircraft towing from preferential gates shall occur only after all common use gates are in use (for the period of use as defined in the Plan), except when the Authority determines after discussion with the Airline that the towing from a common use gate as compared to one of Airline's preferential gates will produce a significant likelihood of further schedule disruption because, for example, operations are not expected to occur exactly as scheduled.

2.05 Adjustment to Gate Use Rights

Airline acknowledges that the Authority may be subject to demands for gate use rights on the Airport from various incumbent and new entrant air carriers and that these demands require an effective

allocation mechanism to ensure maximum efficiency and utilization of gates at the leased premises, gates under the control of Airport Lessees; and the Airport Controlled Gates. Airline and Authority agree as follows:

a) Upon request, Airline shall provide the Authority with gate gate utilization information. This information will include: 1) arrival and departure times for each aircraft (identified by type and owner if not Airline's) using each gate for which Airline has been granted use rights under this Lease; 2) identification of which aircraft remain overnight and which are towed to remote parking positions; and 3) arriving and departing passenger totals by gate for each operation.

b) Upon completion of a comparative analysis of Airline's gates with those of the authority and other Airport Lessees, the Authority may designate Airline as a low utilization carrier among Airport Lessees. In the event that Airport Controlled Gates are found to have a utilization equivalent to or less than that of the three lowest carriers among Airport Lessees, then the Airport Controlled Gates will be considered throughout this Article in the same manner as the premises of Airport Lessees. Authority shall inform Airline of this determination including Airline's relative ranking among other Airport Lessees.

c) After being informed that Airline has been designated as a low utilization carrier among Airport Lessees, Airline may request that Authority provide documentation as to how this determination was made. Authority will provide this information within 30 days of such a request.

d) The following indicies provide examples of the types of measurement the Authority may use in evaluating utilization:

- Passengers per gate for the preceding twelve months;
- Operations (aircraft arrivals and departures) per gate for the preceeding twelve months;
- Average aircraft ground time, excluding overnight aircraft.

In performing such calculations, the Authority shall not consider activities of subtenant airlines which occupy a jetway structured gate position but conduct a ramp loading operation for passengers. The Authority will consider the activities of subtenant airlines which use a jetway for their passenger loading operations.

e) If: 1. A Requesting Airline has requested accommodation of space at Airline's premises.

2. Said Requesting Airline can demonstrate that it has been unable to make arrangements with any Airport Lessee under which it could be accommodated at the Airport, and

3. The Authority has informed Airline that it has received a low utilization designation and the Airline is among the three lowest utilizers among Airport Lessees, and

4. The Authority has determined after discussion with Airline, as the lowest utilization carrier, that the Airline's premises are an appropriate location for the Requesting Airline after giving comparative consideration to compatability of operations with existing tenants, type or character of air service, aircraft type, airport congestion, facility utilization, and the availability of space.

Then: the Airline, in furtherance of the public interest by having the premises fully and most effectively utilized, shall accommodate the request of said Requesting Airline to the extent such request does not specifically compromise Airline's then existing preferential schedule.

If the Airline fails to reach agreement with said Requesting Airline and the Requesting Airline advises the Authority to such effect, the Authority will review the causes of the dispute. If the Authority determines in favor of the Requesting Airline the Authority may instruct the Airline to accommodate the Requesting Airline.

If Airline then fails to accommodate said Requesting Airline, Authority may inform Airline that Airline's gate(s) required by the Requesting Airline will be governed by the Change of Gate status provision of this Lease (See Article 2.06).

f) If Airline is required to enter into an agreement with a Requesting Airline such accommodation may be accomplished by the Airline pursuant to a handling agreement or a sublease. Airline hereby acknowledges that such an agreement shall be subject to the following terms and conditions:

1. The Scheduled Air Carrier may utilize a portion of the leased premises for passenger ticketing, baggage handling and other such activitieis incident to the use of the gate(s). Such accommodation shall take into consideration the then existing utilization of the premises by Airline and any subtenants or other Scheduled Air Carriers already being accommodated including number and time of flights, operations and operating procedures, and aircraft employed by the air carrier seeking accommodation.

The rights of any sublessee airline or Scheduled Carrier to the use of the gates shall be based upon the Common Use Gate provisions of the Plan and shall not be construed to include preferential rights to gates as granted by Authority to Airline by this Lease.

2. The term of the agreement shall not be less than one year and shall require Airline to provide a sixty day notice period for any schedule changes by Airline or by Requesting Airline or both. The agreement shall not be cancelable by Airline unless Handled Airline or Sublessee Airline is in default of any of the terms of the agreement, or at the request of the Authority if after the initial year other Airport premises become available to subtenant that are less utilized than Airline's premises and said available premises are determined by the Authority in its sole discretion to be more appropriate location for subtenant's Airport operations in accordance with Article 2.05(e).

3. The fees charged the Handled Airline or Sublessee Airline by Airline shall be reasonable and non-discriminatory and shall include only the Airline's directly related capital and operating costs for the provision of such services or facilities; a reasonable administrative charge; and related Authority fees imposed on Airline.

4. The agreement shall be subject to the approval of Authority which approval shall not be unreasonably withheld or delayed.

2.06 Change of Gate Status

Airline's preferential use rights as outlined in Article 2.03 of this Lease shall be subject to the following limitations:

A. Upon Airline's failure to accommodate a Requesting Airline, when required by Article 2.05, Authority shall convert an Airline Gate to an Authority Gate.

B. An Authority Gate shall be scheduled and controlled by the Authority except that Airline shall retain the right to schedule its "Base Peak" level of flights on that gate. The term "Base Peak" shall mean the maximum number of times per day that Airline simultaneously occupies, in accordance with the OAG schedule, all of its preferential gates at anytime during the six months immediately preceding the conversion. An example of how Airline and Authority may schedule flights in accordance with the Airline's "Base Peak" is provided as Exhibit ___. Upon conversion to an Authority gate Airline may be required by the Authority to provide access to the gate as well as surrender proportional support space to accommodate ticketing, baggage handling and other activities required with use of the gate. Airline's rent shall be reduced in proportion to the space relinquished. Charges for use of the gates shall be assessed to Airline and other airlines on a non-discriminatory basis in accordance with recognized and reasonable accounting practices employed by the Authority.

D. If, after a period of one-year following conversion to an Authority gate, Airline continues to have a lower utilization rate on the Authority gate than other airlines using the gate, then Authority may designate said gate as a Common Use Gate that will be subject to the Authority's Common Use provisions.

Upon conversion to a Common Use Gate, Airline may require Authority to take back support space in proportion to the gate relinquished by Airline, required for ticketing, baggage handling and other activities necessary to the use of the gate. In the event such space is taken back the Authority will reduce Airline's rent proportionately.

E. At no time shall Airline be allowed to sell, transfer or convey its rights to gates and related areas to any entity other than Authority, except as provided in Article 9. Airline may sell, transfer or convey to the Authority on financial terms that are determined by the unamortized portion of authorized tenant improvements. If Authority elects not to acquire the premises from Airline, then Airline may sell, transfer or convey the premises to another air carrier, subject to the provisions of Article 9 of this lease.

3.04 Additional Rental Terms

(b) No provision of this Lease shall be construed to prevent or prohibit the Authority from assessing Airline for other charges related or incidental to the conduct of Airline's operations at the Airport, including but without limitation, the assessment of landing fee charges for use of the airfield facility. Any such assessment shall be substantially comparable with the rates, rental and other charges imposed on other carriers which make similar use of the airport and which utilize similar facilities, subject to reasonable classifications.

ARTICLE 4 - Rights and Obligations of Airline

For its bridges Airline shall be allowed to charge a reasonable use fee, provided, such fee shall not be excessive in relation to Airline's capital and operating costs for the bridges and gate areas, and shall be subject to the approval of Authority, when said bridges and gates are used by any other carrier on a non-preferential basis. In addition, Airline shall be allowed to charge a reasonable ground power use fee when said ground power is installed by Airline and used by other carriers on a non-preferential basis.

4.14 Domestic Baggage Claim Devices Use by Others

Airline agrees to make available to other carriers its domestic baggage claim devices upon request by the Authority. Airline may charge a reasonable fee for their use and will allow other carriers access to them on a non-preferential basis. Authority recognizes the availability of the devices for others may be limited due to Airline's need to utilize them for its own aircraft.

ARTICLE 8 - Default and Termination.

8.01 Default. If Airline: (1) fails to pay rental, or additional rentals or any other charges due under this Lease within thirty (30) days after receipt of written notice of delinquency, or (2) fails to keep and perform any of the covenants, conditions and agreements herein set forth within sixty (60) days of written notice, and such default in either event not having been cured, at Authority's sole election:

(a) Authority, without terminating this Lease, may re-enter the premises and improve and relet all or any part of it to others, for the account of Airline, and Airline shall promptly reimburse Authority for any deficiency in rentals and additional rentals.

(b) Authority at any time (before or after a re-entry and reletting as provided in (a) above) may terminate Airline's rights under this Lease, and Authority may re-enter and take possession of the premises and cancel all rights and privileges granted to Airline hereunder, without any restriction upon recovery by Authority for past due rentals or other obligations of Airline.

(c) If upon re-entry into the premises under (a) or (b) or for other lawful reason, there remains property of the Airline or any other person upon the premises, Authority may (but without the obligation to do so) remove said personal property and hold it for the owners thereof or may place the same in a public warehouse, all at the expense and risk of the owners thereof, and Airline shall reimburse Authority for any expense incurred by Authority in connection with such removal and storage. Authority shall have the right to sell such stored property provided that it shall give Airline not less than thirty (30) days advance written notice that it intends to conduct such a sale. The proceeds of such sale shall be applied first to cost of sale, second to the payment of charges for storage and removal, and third to the payment of rentals or any other obligation which may then be due from Airline to Authority; and the balance, if any, shall be paid to Airline.

8.02 Termination at Option of Authority. In addition to the causes for termination established in Article 8.01, Authority may terminate this Lease and after ten (10) days written notice to Airline may enter or re-enter the premises (with or without process of law) as if a default had occurred hereunder and not been cured, upon or after the occurrence of any of the following events:

(a) Abandonment for a period of sixty days by Airline of the conduct of its scheduled air transportation business at the Airport.

(b) Termination or suspension for sixty days or longer, by any governmental authority, board, agency or officers of the United States of any certificate, license, permit, or authority held by Airline without which Airline shall not be

lawfully empowered to provide scheduled air transportation services at the Airport.

(c) Entry of a judgment or injunction by any court of competent jurisdiction and the remaining in force thereof for a period of at least sixty days, the effect of which is to prevent or prohibit Airline from providing scheduled air transportation services at the Airport.

(d) Failure of Airline generally to pay its debts under this Lease as such debts become due.

8.03 Termination at Option of Airline. Airline may, at its option, terminate this Lease after ten (10) days written notice to Authority upon or after the occurrence of any of the following events:

(a) Closure of the Airport to all scheduled air transportation services for a period of sixty days or greater.

(b) Except where an article of this Lease confers to Airline a different remedy as sole and exclusive, default by Authority in performance of any of the terms, covenants or conditions to be performed by it hereunder, provided, that Authority shall have failed to remedy or commence the remedying of any said default as promptly as may be reasonably practicable following receipt by Authority of written demand from Airline to do so, which shall in no event be a lesser time to remedy default than thirty days.

ARTICLE 9 - Assignment and Subletting

9.01 Prohibition on Assignment and Subletting. Except with respect to transactions including any carrier as described in Section 9.03, and any requesting Airline which Airline is obligated to accommodate in accordance with the provisions of Article 2.05, and subleases which involve the provision of handling services by Airline as contemplated under 9.02, Airline shall not have the right to sublease all or any portion of the premises. Airline shall not assign, transfer, convey, mortgage, pledge or encumber its interest under this Lease to all or any part of the premises, to any party without the prior written approval of Authority. Any attempted transaction in violation of the provisions hereof shall be null and void and a default hereunder. Without limiting the generality of the foregoing, Authority is expressly entitled to condition its approval as follows:

(i) Airline shall pay Authority as additional rentals 10 percent of Airline's gross revenue from the services and facilities it provides to the other carrier.

(ii) The other carrier shall be required to enter into arrangements with Authority satisfactory to assure the payment of landing fees and otherwise govern the carrier's use of the common use landing field facilities.

(iii) The other carrier shall consent to terms and conditions assuring protection to the interests of Authority which are commensurate with the protections afforded Authority by this Lease.

(iv) The other carrier shall consent to and abide by the Common Use provisions in the Authority's Gate Control and Access Plan if it is granted rights to the use of a gate(s) by Airline.

9.02 Use by Carriers other than Airline.

Airline may use the premises to provide passenger terminal handling services for any other scheduled air carrier certificated in accordance with 49 U.S.C. Section 1301 for the operation of, or incident to, or in connection with the air transportation business performed or to be performed by said carrier. Any such contract, relationship or arrangement, handling agreement, or sub-tenancy relating to such handling services shall be subject to the Authority's prior written consent, which shall not be unreasonably withheld. The Authority may condition its consent, if granted, on payment by Airline to Authority as consent, if granted, on payment by Airline to Authority as additional rentals of up to ten (10%) percent of Airline's gross revenue from the services and facilities it provides to the certificated air carrier including requesting Airlines accommodated by Airline in accordance with Section 2.05 but excluding these carriers described in Article 9.03.

9.03 Authority Consent to Certain Transfers Not to be Unreasonably Withheld.

If, pursuant to Article 9.01, Airline shall request Authority's approval of an assignment, transfer or sublease to a corporation which is Airline's wholly owned subsidiary, a corporation with which Airline shall merge or consolidate, a corporation which may succeed to the air transportation business of Airline, or a wholly owned subsidiary of Airline's parent corporation, Authority shall not unreasonably withhold its consent. It shall not be unreasonable for Authority to require security for payment of rentals and performance of all obligations provided in this Lease.

9.04 Assignment and Subletting not to be inconsistent with this Lease.

The provisions of any and all assignments[,] transfers, subleases, handling agreements and other agreements allowed under Article 9, hereunder shall not be inconsistent with the terms and provisions of this Lease and Agreement.

9.05 Assumption or Assignment in Bankruptcy. Article 9.01 shall not apply to any valid assumption or assignment of this Lease of all or part of the premises by a Trustee or the Airline as a debtor in possession, under Section 365 of the Bankruptcy Code of 1978, as

amended, provided, that adequate assurance of future performance for the purposes of the assumption or assignment of this Lease shall include, but shall not be limited to:

(a) Adequate assurance of the reliability of the proposed source for the rental payments due under this Lease upon the assumption or assignment of this Lease,

(b) Adequate assurance that all other consideration due under this Lease shall be forthcoming after the assumption or assignment of this Lease.