AirTAP Briefings

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A primer on airport finance

Editor's note: This article gives a general overview of the budget process for small airports. For a more in-depth look at the topic, see ACRP Report 16, Guidebook for Managing Small Airports, *available online at http://onlinepubs.trb.org/onlinepubs/acrp/acrp_rpt_016.pdf.*

Developing and implementing an accurate budget is a basic tenet of airport finance. It allows an airport manager to plan the dollar amounts required to operate and maintain an airport for a defined period of time. Coordinated long-term planning is also needed to determine capital expenditures such as runway construction, land acquisition, or major equipment purchases. Forms of budgeting vary, often depending on the style adopted by a larger governmental entity such as a city, which typically follows a line-item budget, program budget, or activity budget format.

The airport manager normally prepares airport operations budgets for a one-year fiscal period. Two of the most important steps in this process are to identify income sources and identify expenses.

Income Sources

Revenue generation should provide for an economically self-sustaining airport operation. Airport revenue sources are generally tied to operating or rental agreements. However, revenue generated at a small general aviation airport is typically limited, and therefore often supplemented with governmental aid. Other sources of airport revenue include:

- Commercial land leases and rents
- T-hangar lease agreements
- Private hangar land lease
- Agricultural land lease
- Terminal concession rents
- Fuel flowage fees
- Landing and ramp fees

Fuel sales is the most common revenue source, followed by land leases, T-hangar leases, and rent. Other sources are industrial park revenues, advertising, parking fees, rental car revenues, terminal concessions, commercial land development, and residential or office rent on airport property.

Additional information on revenue generation can be found in a recently published ACRP synthesis, *Innovative Finance and Alternative Sources of Revenue for Airports*, available online at http://onlinepubs.trb.org/onlinepubs/acrp/acrp_syn_001.pdf.

Some airport operators (typically at large- or medium-hub airports) use municipal bonds. Many airports have maintained investment-grade ratings from credit rating agencies. In addition, some airport operators use bond and grant anticipation notes, pooled credit programs, and capital leases. These operators also carry reduced interest rates on outstanding bonds and manage interest rate risk by entering into interest rate swaps with investment banks. Although most airports do not have bonding authority, their associated municipality may.

Leasing and Use Agreements

Leasing and use agreements often provide a significant source of income, so an airport manager ought to be familiar with the types used at small airports. Airport leases are considered either commercial or noncommercial use agreements. An array of other leases may also be present at an airport facility, such as for agricultural operations or other non-aviation uses.

The application and enforcement of lease administration and policy must be consistent. Airport sponsors of federally obligated airports must also ensure that certain grant obligations are being met with regard to airport leasing policy.

Terms and conditions. An airport manager must carefully consider the terms and conditions incorporated into an airport lease agreement, especially regarding commercial use. The airport representative should negotiate terms consistent with other airport leases, goals, and objectives, with the understanding that the commercial tenant may be contemplating a significant investment at the airport. The terms of the lease must also be consistent with the master plan for phased airport development and land use.

Airport lease agreements should also specify permitted uses and premises to be leased, establish rental rates and payments, and spell out the responsibilities of each party. Other conditions of the lease should provide for required insurance, subleasing, and termination. It is also important that the agreement cite the applicable operating standards, codes, ordinances, or policies of the airport.

The airport manager must establish a lease policy that allows for standardization among tenants engaged in similar activities. Federal sponsor requirements should be part of the airport lease agreement, which includes language pertaining to nonexclusive rights, use of airport, nondiscrimination, and airport commitments to federal or state agencies.

Minimum standards. If an airport allows businesses to conduct commercial operations and other aeronautical activities from the airport, it must identify reasonable criteria for the accommodation of commercial aeronautical services. The FAA encourages operators of public-use airports to develop minimum standards to promote safety in all airport activities, maintain a higher quality of service for airport users, protect the public from unlicensed and unauthorized products or services, enhance the availability of adequate services for all airport users, and promote the orderly development of airport land.

Minimum standards establish a set of requirements to accommodate a range of commercial activities, such as aircraft maintenance, fueling, charter, flight training, aircraft sales, rental, and parts. They are often made part of an airport's commercial leases, addressing requirements such as intended scope of activities, site development standards, personnel experience, financial stability, and insurance. The standards also ensure that each like operator is meeting the same basic criteria and that the airport is not giving any one operator an advantage over others.

An airport ought to consider a variety of factors when establishing minimum standards, including the particular nature of anticipated commercial activities and the

Learn more at the Fall Forum!

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Want to brainstorm more ideas for generating revenue? Then attend the session "Is an Air Show in Your Future? Finding Ways to Bring Money and People to Your Airport" at this year's AirTAP Fall Forum. Brian Ryks, Duluth International Airport executive director, will share interesting ways he has brought funding and support to his airport, while Sandy DePottey, FAA, will talk about rules and processes related to generating and spending revenue. The Fall Forum will be held October 7 and 8 at the Arrowwood Resort in Alexandria. Register and find more details on the AirTAP Web site at http://www.airtap.umn.edu/Events/FallForum/2010/index.html.

operating environment at the airport. FAA Advisory Circular 150/5190-5 suggests considering the following questions:

- What type of airport is at issue? Will the airport provide service to small general aviation aircraft or will it serve air taxi operators as well?
- What types of aeronautical activities will be conducted at the airport, and is there a demand for them?
- How much space will be required for each type of aeronautical activity that may potentially operate at the airport?
- What documentation will business applicants be required to present as evidence of financial stability and good credit?
- To what extent will each type of aeronautical activity be required to demonstrate to the sponsor compliance with sanitation, health, and safety codes?
- What requirements will be imposed regarding minimum insurance coverage and indemnity provisions?
- Is each minimum standard relevant to the aeronautical activity for which it was designed to apply?

Airport managers should develop minimum standards flexible enough to adapt to changing conditions in the airport environment and should review them periodically. Standards must not attempt to accommodate a single operator or establish unreasonable criteria that may lead to a service monopoly. Consistent application of the standards will reduce potential conflict and promote orderly airport development. Airport managers can contact their local FAA Airports District Office for assistance in developing reasonable minimum standards.

Rates and charges. No set guidelines or standards exist for what individual airports should charge tenants, but rates should reflect the cost of providing the facility, maintaining and administrating the facility, recovering capital expenditures, and any other costs associated with the airport operation.

It is not always practical to charge for only those facilities or services received. Most users of the airport facility will also take advantage of common-use areas as well as airport-maintained airside facilities and navigational aids.

A common method of establishing rates and charges is by researching what neighboring airports are charging for like services and facilities. The difficulty in using this approach is that the outcome may not accurately reflect the actual costs of providing the facilities or services. Another approach, referred to as the compensatory approach, is based on cost recovery for actual costs of facilities and services.

In most cases, airport owners can apply a combination of both market-based pricing and cost-recovery pricing to determine rates and charges. The way fees are set also depends largely on the structure of airport leases. Short-term agreements allow management to adjust rates more frequently as required, whereas long-term contracts may not. Therefore, it's fairly common to establish rate escalators in longer-term lease arrangements. The FAA recommends that all leases with a term exceeding five years provide for periodic review of the rates and charges for the purpose of adjustments to reflect current values.

Rates may also be established for terminal, airfield, and buildings and grounds charges. Terminal charges include such things as use of conference facilities, concessions, gift shops, car rentals, or office space fees. Airfield charges include fuel flowage fees and landing and ramp fees. These fees may be collected from private commercial operators as part of the lease agreement.

Liability and insurance. An airport must be protected with adequate airport liability insurance. Airports and their tenants have the same general type and degree of liability exposure as the operator of most public premises. Types of insurance coverage include Basic Airport Premises Liability, Products Liability/Completed Operation Liability, and Hangar Keepers Coverage.

Other examples of coverage are liability insurance for airport events and personal and advertising injury liability. Satisfactory insurance requirements and provisions for indemnification and workers' compensation must be contained within airport lease agreements. The airport lease policy may also provide that the airport owner is named as additionally insured. The airport owner should review lease insurance requirements periodically with his or her insurance providers, risk managers, and attorneys.

Airport Expenses

Expenses for small airports include capital improvements, operating expenses, and non-operational expenses. Some sources of operating expenses are labor, supplies, utilities, and maintenance costs that are incurred on a day-to-day basis. The structure of an airport operation within a municipal organization varies, and many actual expenses are difficult to measure. If staff is shared across departments, labor costs at the airport may be hidden within another department's budget. Accurately identifying those costs is an important part of the budgeting process.

The accounting of non-operational expenses also depends on the position of the airport within the city, county, or organization that actually owns the airport. These costs, which may result from such things as equipment depreciation and debt service on existing airport financial obligations, must be considered when developing the budget. An airport manager may need assistance from the city clerk or another accounting staff member to identify the actual costs assigned to the airport budget.

Capital improvements are those projects that must be planned and budgeted for over a specified time period. In-depth information about developing a Capital Improvement Plan (or CIP) is provided in the *Capital Improvement Program Guide*, located online at http://www.airtap.umn.edu/pdf/CIP_guide.pdf.

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