PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA
ACTION ITEM

Item No. 6a

Date of Meeting September 10, 2013

DATE: September 3, 2013

TO: Tay Yoshitani, Chief Executive Officer

FROM: Mark Reis, Managing Director, Aviation
Michael Ehl, Director, Aviation Operations
James Jennings, Manager, Aviation Properties

SUBJECT: 2013-2017 Signatory Lease and Operating Agreement between the Port and the Airlines operating at Seattle-Tacoma International Airport ("Airport")

ACTION REQUESTED

Request Commission authorization for the Managing Director, Aviation Division ("Managing Director") to (1) execute a 2013-2017 Signatory Lease and Operating Agreement ("SLOA III") between the Port and signatory airlines for the use of facilities at the Airport and (2) to suspend the implementation of rates and charges and other provisions of Resolution No. 3677 no earlier than upon commencement of said SLOA III.

SYNOPSIS

On December 31, 2012, the 2006-2012 Signatory Lease and Operating Agreement ("SLOA II") expired. Due to an impasse in negotiations for SLOA III, Commission adopted Resolution No. 3677 on May 14, 2013, establishing a rates and charges methodology for the use of facilities at the Airport in accordance with applicable federal Department of Transportation ("DOT") requirements. The Commission further authorized the Managing Director to suspend implementation of the Resolution in the event Port staff and the airlines reached agreement on a SLOA III prior to July 1, 2013. On July 1, 2013, the Managing Director implemented the airline rates and charges in accordance with Resolution No. 3677.

Subsequently, Alaska Airlines, as chair of the Airline Airport Affairs Committee ("AAAC"), and Port staff re-engaged in lease negotiations. The following business terms associated with SLOA III are the result of those negotiations.

The term of SLOA III will commence on January 1, 2013, only if (a) four (4) carriers accounting for fifty percent (50%) of the terminal rents and landing fees paid to the Port in 2012 by all air carriers operating at the Airport execute and deliver the agreement to the Port by November 15, 2013, and (b) at least an additional six (6) other air carriers either execute and deliver the agreement or provide the Port with written documentation recommending the agreement to their respective boards by November 15, 2013, so that carriers accounting for sixty six and two-thirds percent (66 2/3%) of the terminal rents and landing fees paid to the Port in 2012 by all air carriers operating at the Airport have either executed SLOA III or provided documentation to the port by November 15, 2013, demonstrating their management's recommendation to do so. Otherwise, the rates and charges and other provisions under Resolution No. 3677, as implemented by the Managing Director, will remain in effect for 2013.

LEASE SUMMARY COMPARISON

Provision	SLOA II	SLOA III
Term	7 Years	5 Years
Debt Service Coverage	Included in Airline Rate base(s) if overall airport debt service coverage falls below 1.25 times.	No change.
Revenue Sharing	None	Port will share with airlines 50% of net revenues in excess of 1.25x debt service.
Insurance	$300M aviation liability; $10M auto.	$500M aviation liability; $10M auto.
Security Deposit/ Security Fund	Security Fund retained by Airport equal to 1/12 of revenue requirement for Airfield and Terminal. New entrants provide security deposit or buy into Security Fund.	Security Fund eliminated. If SLOA III executed in 2013, airline revenue requirement in 2013 will be reduced by an amount equal to Security Fund balance. No surety required for carriers operating in good financial standing at the Airport for at least 24 months.
Cost of Vacant Space	Airport recovers full cost of all aeronautical space, including vacant space.	Airport assumes cost of vacant space for publicly accessible offices and airline clubs.
Majority-in-Interest (MII) Approval of Capital Projects	Negative MII vote requires six month delay.	Negative MII vote requires 12 month delay.
Amortization	Amortization charged to rate base for aeronautical assets placed in service beginning in 2006 at 6.0%.	Amortization charged to rate base for aeronautical assets placed in service beginning in 1992 at rate that reflects borrowing costs in year asset placed in service.
Space Categorization/ Weights	Gates & Ticket Counters (2.5) Offices (1.5)	Gates (2.0) Ticket Counters, public-accessible

	Baggage (makeup, pickup, and FIS) (1.0) Closed Storage (0.5)	offices (including VIP lounges), and baggage (makeup and pickup) (1.0) Non-publicly-accessible offices (0.5) Closed Storage (0.25)
Federal Inspection Services (FIS)	Not separate cost center. Discretionary use of non-airline revenues to reduce revenue requirement.	Separate cost center, including share of baggage system costs. Rate set to recover costs.

BACKGROUND

Port staff began negotiations with a committee of Airline representatives in November 2011. These lease negotiations continued through June 2012 when it became apparent that the Port and the airlines had significant, and at the time, insurmountable differences in negotiation positions. The Port began consideration of an airline rate resolution in lieu of a negotiated agreement, and after consultation with the Commission, analyzed this alternative between June and August 2012. In August through October 2012, the Port and the airlines discussed the possibility of a one-year extension to SLOA II to allow the parties additional time to negotiate. In October, the airlines instead demanded the Port implement rates and charges by resolution. Port staff developed and refined rates and charges by resolution between October 2012 and February 2013. When the airlines saw the resolution rates, they requested to restart negotiations. Negotiations broke down again, and the Commission authorized implementation of Resolution No. 3677 in May 14, 2013. On July 1, 2013, Port staff issued notice to all airlines operating at the Airport of the rates and charges to be levied under Resolution No. 3677. In July, negotiations resumed, resulting in the proposed SLOA III.

The term of the agreement commences on January 1, 2013, only if both of the following conditions are met:

- At least four air carriers execute the agreement by November 15, 2013. These air carriers must account for at least 50% of the total terminal rents and landing fees paid to the port in 2012 by all air carriers operating at the Airport; and
- A minimum of 6 additional air carriers must provide to the port by no later than November 15, 2013, written documentation that their management intends to recommend to their boards execution of the agreement, so that that the total of air carriers either executing the agreement or providing written recommendations to their boards to do so account for at least sixty-six and two-thirds percent (66 2/3%) of the total amount of terminal rents and landing fees paid to the port in 2012 by all air carriers operating at the Airport.

If these conditions are not met, the rates and charges and other provisions of Resolution No. 3677, as implemented by the Managing Director, will remain in effect for 2013.

FINANCIAL IMPLICATIONS

This lease agreement will define the methodology for setting airline rates and charges that will amount to approximately $1.3 billion in operating revenues for the Airport during the term of this agreement (2013 – 2017). Key financial provisions include: 1) Debt service coverage trigger: permits the Airport to include in the airline rate base debt service coverage up to 25% of debt service as needed to bring total Airport debt service coverage up to 1.25x. This ensures that the Airport will maintain at least 1.25x debt service coverage and 2) Revenue sharing: the Airport will share 50% of net revenues in excess of 1.25x debt service with the airlines. This permits airlines to benefit from increased Airport income through a reduction in airline fees.

STRATEGIES AND OBJECTIVES

SLOA III supports the Port's Century Agenda objective of meeting the region's air transportation needs at Sea-Tac for the next 25 years by creating a financial structure that permits the Airport to generate adequate cash flow to maintain and invest in new facilities while also sharing revenues with the airlines to reduce airline costs.

It also supports the Airport strategy of reducing airline costs as far as far as possible without compromising operational and capital needs.

ALTERNATIVES AND IMPLICATIONS CONSIDERED

Alternative 1) – Do nothing. Resolution No. 3677 would remain in place and would control the financial and operating relationship between the Port and the airlines. Under this alternative, it is possible that at least two airlines, Alaska Airlines and Southwest Airlines, would file formal complaints against the Port with the U.S. Department of Transportation. This is not the recommended alternative.

Alternative 2) – Authorize execution of SLOA III. **This is the recommended alternative.**

ATTACHMENTS TO THIS REQUEST

- 2013-2017 Signatory Lease and Operating Agreement

PREVIOUS COMMISSION ACTIONS OR BRIEFINGS

- May 14, 2013 – The Commission adopted Resolution No. 3677, as amended, setting rates and charges for Airlines operating at the Airport.
- April 23, 2013 – The Commission approved First Reading of Resolution No. 3677, setting rates and charges for Airlines operating at the Airport.
- April 2, 2013 – Staff requested First Reading of Resolution No. 3677. The Commission postponed action to April 23, 2013 to allow more time for Port staff and airlines to negotiate a lease agreement.