

PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA
ACTION ITEM

Item No.	<u>6c</u>
Date of Meeting	<u>March 10, 2015</u>

DATE: March 2, 2015
TO: Ted Fick, Chief Executive Officer
FROM: Michael Ehl, Director Aviation Operations
Kazue Ishiwata, Senior Manager Air Service Development
SUBJECT: Revised Incentive Program for New Small Community Air Service for Seattle-Tacoma International Airport

ACTION REQUESTED

Request Commission authorization for the Chief Executive Officer to implement a revised incentive program for new commercial air service for Seattle-Tacoma International Airport to enhance its Category E - Small Community Air Service for unserved destinations in Washington, Oregon, and Idaho through fee waivers and the inclusion of promotional funding consistent with Categories A-D of the Airport's overall air service incentive program.

SYNOPSIS

The primary purpose of this action is to enhance the Airport's incentive program for new commercial air services, specifically for small community airports in the Pacific Northwest, with a goal to attract airlines to establish critical links between Seattle and smaller regional communities.

No airlines have taken advantage of the previously authorized incentive program for small community air service since the Commission initially implemented the program in 2007, while the industry's economic environment for the market has grown even more challenging.

The proposed modification is aimed to increase the ability to attract service on economically challenging but valuable routes to small community airports in the Pacific Northwest by temporarily waiving landing fees and certain facility charges, and by providing joint promotional funds. The program is designed to mitigate the risk for prospective airlines by providing estimated annual benefits of \$200,000 to \$434,000, depending on the level of service. The program elements of Categories A through D in the New Air Service Incentive Program will remain unchanged.

BACKGROUND

For many communities in the Pacific Northwest, air service to Seattle-Tacoma International Airport is a critical link to the global transportation network. However, air service from other Washington airports to Seattle has steadily declined in recent years. In 2000, there were nearly

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42,000 annual scheduled passenger departures to eleven Washington airports; by 2005, the number had halved to just over 20,000 departures to eight Washington airports. The economic downturn that followed further deteriorated the small community air service environment, and in 2015 the annual scheduled departures decreased to less than 15,000 to seven Washington airports.

Smaller airports nationwide have faced similar challenges due to fundamental shifts in airline economics over the past two decades and to the lack of an economically viable small aircraft to serve smaller communities. Most major U.S carriers are removing smaller, inefficient 37-50 seat aircraft from their fleets entirely. Communities around the nation are working hard to find solutions to improve air service to a broad section of the traveling community, provide better access from secondary markets to the national and international air transportation system, and to develop strategies for improving air service.

PROJECT JUSTIFICATION AND DETAILS

In recognition of the difficulties faced by small Pacific Northwest communities in attracting viable air service, the Airport is proposing to enhance Category E of the previously authorized New Air Service Incentive Program. The modification will allow prospective airlines to reduce the risks of beginning such services, particularly the high start-up costs associated with new services. The program provides participating airlines with temporary waivers of landing fees and certain facility charges, as well as joint promotional support designed to assist the establishment of new services in their first two years.

Project Objectives

To develop vital air service links between the Airport and the Pacific Northwest's small community airports in order to stimulate and facilitate the region's growing economy and to enhance the role of the Airport as the regional hub. The incentives are designed to alleviate cost pressures on new services as they establish local operations and assist in the development of a visible presence in the market.

Scope of Work

The previously authorized New Air Service Incentive Program includes five categories under which a prospective route can qualify for the Airport's incentives. Small community air service is designated as Category E of the New Air Service Incentive Program, and includes air service to an unserved destination in Washington, Oregon, and/or Idaho.

Proposed changes to the Category E incentives affect Parts II and III of the New Air Service Incentive Program. The Part I Incentive (Discounted International Arrival Facility Charges) is not applicable to Category E services.

Part II Incentives for Category E have been updated to include full waivers of landing fees, gate/lobby fees, and ticket counter fees for the first two years of service. Previously, ticket counters were not included as part of the incentive program.

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Fee/Charge	Duration	Existing Part II Incentive Category E	Proposed Part II Incentive Category E
Landing Fee Waiver	2 years	100%	100%
Gate/Lobby Fee Waiver	2 years	100%	100%
Ticket Counter Fee Waiver	2 years	-	100%

* The second year of eligibility for Category E small community air services is contingent upon the air carrier meeting a minimum of 75% of their projected operations in the first year of the program.

Part III Incentive: Joint Promotion Program

Part III Incentives have been introduced for Category E for the first time. Eligible services will receive \$12,000 per year for the first two years of service to assist in promoting the service and developing a visible market presence.

Incentive	Duration	Existing Part III Incentive Category E	Proposed Part III Incentive Category E
Joint Promotional Fund	2 years	-	\$12,000 per year

Eligibility

Eligibility for Category E services has been expanded to allow services with a minimum of five flights per week (reduced from a minimum of daily service), and to allow carriers to qualify for the incentive program if the same carrier has not served the route for at least 18 months (reduced from a minimum of 36 months).

To be eligible as a new small community air service for Category E, the route must be:

- A nonstop service for unserved destinations in Washington, Oregon and Idaho;
- A minimum of five scheduled round trips each week via any aircraft type;
- Year-round scheduled service sold to the public;
- Not served by the same carrier or its subcontract partner carrier previously and canceled within 18 months;
- Not considered a replacement service of another service previously served by profit-sharing Joint Venture agreement carrier on the same city pair.

Schedule

To be eligible for this incentive program, the new air service must be announced and become publicly available prior to the termination of the current Signatory Lease and Operating Agreement (SLOA). The current SLOA includes provision of the incentive program for

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passenger air services. However, the carrier does not have to be a signatory carrier to be eligible for the incentive benefit per the Federal Aviation Administration guidelines for the incentive program.

FINANCIAL IMPLICATIONS

Financial Analysis and Summary

Fee Waiver Example:

Aircraft: 76-seat Bombardier DHC8-Q400

Frequency: 1 flight per day

Airport Charges	SLOA Signatory Carrier Rate	Standard Annual Cost to Existing Carrier	Additional Annual Costs for New Entrants	Waived Amount	Estimated Cost Paid by Airline
Landing Fee	\$3.48 per 1,000 lbs	\$78,752		\$78,752	\$0
Gate/Lobby	\$246.72 per turn	\$90,053		\$90,053	\$0
Ticket Counters	\$21.62 per position per hour	\$31,565		\$31,565	\$0
Ramp Tower Fee	\$8.63 per landing	\$3,150		-	\$3,150
Passenger Airline Apron Fee	\$0.41 per 1,000 lbs	\$9,278		-	\$9,278
Bag Claim Device Charge*	\$146,686 per carrier		\$146,686	-	\$146,686
Bag Claim Fee	\$0.96 per deplaned pax	\$21,305		-	\$21,305
Baggage Makeup System Fee	\$1.20 per outbound bag	\$26,630		-	\$26,630
Baggage Makeup Device Charge*	\$60,436 per carrier		\$60,436	-	\$60,436
Baggage Makeup Device Fee	\$3.91 per outbound bag	\$86,771		-	\$86,771
Total for Existing Carriers		\$347,504		\$200,370	\$147,134
Total for New Entrant Carriers			\$554,626		\$354,256

Notes:

- Rates assume carrier is a signatory to the Airport's Signatory Lease and Operating Agreement (SLOA); non-signatory carriers pay higher rates but are exempt from charges marked with an asterisk (*).
- Carriers with existing leased preferential gates and ticket counters are eligible for fee waivers only if they use common-use facilities for the new service.
- Ticket Counters: assumes 4 ticket counter hours per turn
- Bag Claim Fee: assumes 80% load factor to estimate passenger numbers
- Baggage Makeup System and Device fees: assumes 1 bag per passenger

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Fee Waiver Example:

Aircraft: 9-seat Cessna Caravan

Frequency: 3 flights per day

Airport Charges	Non Signatory Rate	Standard Annual Cost to New Entrant Carrier	Waived Amount	Estimated Cost Paid by Airline
Landing Fee	\$4.35per 1,000 lbs	\$37,153	\$37,153	\$0
Gate/Lobby	\$308.40 per turn	\$337,698	\$337,698	\$0
Ticket Counters	\$27.03 per position per hour	\$59,196	\$59,196	\$0
Ramp Tower Fee	\$10.79 per landing	\$11,815	-	\$11,815
Passenger Airline Apron Fee	\$0.51 per 1,000 lbs	\$4,356	-	\$4,356
Bag Claim Device Charge*	n/a per carrier	\$0	-	\$0
Bag Claim Fee	\$1.20 per deplaned pax	\$9,461	-	\$9,461
Baggage Makeup System Fee	\$1.50 per outbound bag	\$11,826	-	\$11,826
Baggage Makeup Device Charge*	n/a per carrier	\$0	-	\$0
Baggage Makeup Device Fee	\$4.89 per outbound bag	\$38,553	-	\$38,553
Total		\$510,058	\$434,037	\$76,011

Notes:

- No existing carrier at the Airport currently utilizes a Caravan in its fleet, necessitating a new entrant carrier
- Rates assume carrier is not a signatory to the Airport's Signatory Lease and Operating Agreement (SLOA). Non-signatory carriers pay higher rates but are exempt from charges marked with an asterisk (*)
- Ticket Counters: assumes 2 ticket counter hours per turn (6 per day)
- Bag Claim Fee: assumes 80% load factor to estimate passenger numbers
- Baggage Makeup System and Device fees: assumes 1 bag per passenger

Examples above do not include additional expected income from indirect revenues such as Passenger Facility Charges or Airport Dining and Retail.

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STRATEGIES AND OBJECTIVES

This project supports the Century Agenda objective to advance this region as a leading tourism destination and business getaway by making Seattle-Tacoma International Airport the West Coast “Gateway of Choice” for international travel.

This project also addresses the Aviation Division’s strategic objectives to become one of the top ten customer service airports in North America and to operate a world-class international airport by ensuring safe and secure operations and by anticipating the meeting needs of tenants, passengers and the region’s economy.

ALTERNATIVES AND IMPLICATIONS CONSIDERED

Alternative 1) – Maintain Existing Incentive Program As Is

This alternative would maintain the New Air Service Incentive Program in its current state, with no modifications made to any incentive category. This is not the recommended alternative.

Pros:

- Does not require any additional financial commitments for new services beyond those in the current Commission-approved New Air Service Incentive Program.

Cons:

- Effectiveness of the incentive quality in Category E services is highly questionable, since no carriers have participated in the program for a Category E service despite the program’s implementation since 2007, presumably due to the inability of the incentives offered to sufficiently mitigate risk to the carrier.

Alternative 2) – Expand Category E Incentives and Expand Eligible Communities

This alternative would not only expand the benefits given under the Category E incentive program, but would also expand the eligibility of the program to include Pacific Northwest communities that currently have limited services to the Airport. This is not the recommended alternative.

Pros:

- The incentive is more attractive to the carriers with reduced risks for the start-up operation.
- Expanding the support to the community with limited air services would stabilize vulnerable operations.

Cons:

- For the Airport to provide incentives to services that are currently in place is considered a “subsidy” and is expressly forbidden by the FAA’s guidelines on Air Service Incentive programs in violation of the revenues diversion prohibition.
- Overly generous incentive program has the tendency to attract an unsustainable new service only for the duration of the fee waivers and terminal rent discount.

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- Providing incentives solely to new entrant carriers to existing markets would likely weaken the financial viability of both services, and would not further the goals of the small community incentive program.

Alternative 3) – Expand Category E Incentive Benefits for Unserved Destinations

This alternative expands the incentive benefits for the participating airline under the Category E incentive program, but limits the eligibility to previously unserved new routes. **This is the recommended alternative.**

Pros:

- This modification enhances the benefits for the prospective carrier and serves as the final inducement in their decision-making process with reduced financial risk to operate small community air services, and adheres to the guidelines on incentive programs as set forth by the FAA.

Cons:

- While the modification to the incentive program is not excessively generous, there is still a risk of potentially lost revenues if the service is not sustainable beyond the incentive period.

ATTACHMENTS TO THIS REQUEST

- Seattle-Tacoma International Airport New Air Service Incentive Program, proposed March 2015 version

PREVIOUS COMMISSION ACTIONS OR BRIEFINGS

- September 27, 2011 – the Commission authorized revision to the incentive program to include a new category for ultra-long-haul international operations.
- June 28, 2011 – the Commission approved a revised incentive program consistent with recently-published Federal Aviation Administration guidelines on airport incentives.
- June 14, 2011 – the Commission was briefed on the growth of international air service in recent years.
- May 5, 2009 – the Commission authorized revision to the incentive program to include a narrow-body international air service to Europe, previously not included in the category.
- November 2, 2007 – the Commission authorized a modification to the previously approved program by allowing the Joint Promotion Program's fund to be utilized with greater flexibility within the existing cost and timeline limit in multi-years, eliminating the previously defined per-year usage limit.
- **April 27, 2007 – the Commission authorized the implementation of a small community air service incentive program.**
- April 10, 2007 – the Commission authorized revision to the incentive program to include trans-border commercial air service routes at a different benefit level.
- February 16, 2007 – the Commission authorized modifications to the first request of the incentive program and raised the maximum benefit to an air carrier.

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- December 13, 2005 – the Commission authorized the first request for implementing a new international air service incentive program.