PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA
STAFF BRIEFING

Item No. 7d

Date of Meeting May 17, 2016

DATE: May 11, 2016

TO: Ted Fick, Chief Executive Officer

FROM: R. Borgan Anderson, Director, Aviation Finance & Budget

SUBJECT: Aviation Plan of Finance Update

SYNOPSIS

Consistent with commission guidance in the May 26, 2015 motion regarding the funding of the Aviation Division Capital Improvement Plan (2015 Funding Motion), staff is providing the commission an update on the funding plan and the implications for future airline rates and passenger airline cost per enplaned passenger (CPE). In October of 2015, when the 2016 capital budget and plan of finance was presented to the commission, there was uncertainty over the final cost estimates of major projects such as the International Arrivals Facility (IAF) and the North Satellite Expansion (NSAT). This uncertainty negated the value of future rate analysis at that time.

The Aviation Division's capital program for 2016 – 2025 anticipates spending $3.4 billion. The plan includes spending over $2 billion on four projects: IAF, NSAT, Baggage Optimization and South Satellite renovation (SSAT). Since the airport sets airline rates to recover costs (capital and operating costs), there will be cost pressures driving rates up in the years to come. It should be noted that while the capital plan includes allowances for as yet unidentified projects, it does not explicitly incorporate investments needed to implement the Sustainable Airport Master Plan.

Passenger Facility Charge revenues (PFCs) are an important funding source and a key tool to manage airline rates because all costs paid with PFCs are excluded from airline rate bases. The base funding plan assumes that 100% of the revenue bond debt service associated with the construction of runway 16R/34L (Third Runway, placed in service in 2008, total cost approximately $1 billion) is paid with PFCs to manage the landing fee rate. With the planned expenditures on the NSAT and SSAT projects, the projected terminal rental rate will increase 65% by 2025, while landing fees are expected to increase by only 5.6%. By shifting the use of PFCs, the Port could moderate the growth in terminal rents while allowing the landing fee rate to increase. The attached PowerPoint presentation shows the future rate impacts for the base case and two additional scenarios that incorporate such shifts. Staff has begun discussions with the airlines to determine their preferences. No definitive decision is needed at this time.

BACKGROUND

Consistent with the 2015 Funding Motion, staff has developed a funding plan that aims to maintain a competitive landing fee, Federal Inspection Services rate (FIS, the international arrivals fee charged to airlines) and CPE compared to peer airports. While not mentioned specifically in the 2015 Funding Motion, maintaining competitive terminal rents is also important. The significant investments the Port will be making in terminal improvements (approximately $1.1 billion for NSAT and SSAT) will drive up terminal rents. Staff is analyzing through scenario analysis the future rate impacts of shifting PFCs from the airfield cost center to the terminal and FIS cost centers as follows:

		Scenario 1		**Scenario 2**		**Scenario 3**	
Rate Category	2016 Rate	2025 Rate	2016-25 % Change	2025 Rate	2016-25 % Change	2025 Rate	2016-25 % Change
Landing fee	3.57	3.77	5.6%	4.61	29.1%	4.61	29.1%
Terminal Rents	118.89	196.68	65.4%	178.60	50.2%	180.00	51.4%
FIS	5.76	12.00	108.3%	12.00	108.3%	10.00	73.6%
CPE	11.00	15.40	40.0%	15.44	40.4%	15.44	40.4%

Scenario 1 is the base case, and reflects two key assumptions: 1) 100% of Third Runway revenue bond debt service is paid with PFCs, and 2) Sufficient PFCs are used to pay revenue bond debt service on the IAF to achieve a $12 FIS rate (highest projected rate among peer airports). All remaining PFCs go to terminal projects. Scenario 2 begins shifting PFCs from the airfield to the terminal cost center in 2019, allowing the landing fee to grow 3% per year. The PFCs are applied to paying terminal revenue bond debt service to achieve a reduction in the percent increase in terminal rents from 65% to 50%. Scenario 3 shows a further shift of some PFCs from the terminal cost center to the FIS cost center to achieve a $10 FIS rate rather than $12. Since the FIS cost center is small compared to the terminal, a modest shift of PFCs can reduce the FIS rate increase from 108% to 74%, while causing the terminal rate to change by only 1%.

In 2015, much of the dialogue with the commission and the airlines relating to funding focused on specific funding plans for individual projects (e.g., IAF and NSAT). While project funding plans are the building blocks for future rates, it is the future rates that are truly important. The following tables show the funding plans for the NSAT and IAF projects corresponding to Scenario 1 (base case). The shifts in use of PFCs for Scenarios 2 and 3 do not change the project funding plans; rather, the changes are reflected in alternative uses of PFCs to pay revenue bond debt service by cost center once the projects are completed, thus altering the costs that are recovered, and the rates charged to airlines.

NSAT Funding plan, Base Case:

Funding Sources	$000s	Capital Rate Base	2020	2024
Cash/ADF	537	Amortization	36	36
Revenue Bonds	408,071	Debt Service	11,886	34,164
PFCs	122,493	DS paid w/PFCs	(3,176)	(20,870)
Total	531,102	Net capital costs	8,746	13,330
Effective percent of PFCs to fund project costs:			43.6%	70.0%

At this time, staff is assuming for planning purposes that 70% of the costs of NSAT will be eligible for use of PFCs. The actual eligibility percentage will be determined by the Federal Aviation Administration. In Scenario 1, maximum PFC funding is achieved in 2024. For comparison, under Scenario 2, maximum PFC funding would be achieved in 2022.

IAF Funding Plan, Base Case:

Funding Sources	$000s	Capital Rate Base	2020	2024
Cash/ADF	200,000	Amortization	-	-
Revenue Bonds	308,365	Debt Service	28,932	28,947
PFCs	100,000	DS paid w/PFCs	(18,427)	(19,778)
Total	608,365	Net capital costs	10,505	9,169
Effective percent of PFCs to fund project costs:			48.7%	51.1%

Consistent with commission direction, the funding plan for the IAF includes up to $200 million cash (Airport Development Fund) without including an annual amortization charge in the FIS rate base. For planning purposes, staff has assumed that 80% of the IAF costs would be eligible for use of PFCs. As with NSAT, the actual eligibility percentage will be determined by the FAA. Since the funding plan targets a $12 FIS rate, the Port uses only sufficient PFCs to achieve that rate.

Staff presented these concepts to the airlines at the March 15, 2016 Airport Airline Affairs Committee (AAAC) meeting. There is a special AAAC meeting scheduled for May 3, 2016 to discuss the above in greater detail.

Comparisons to peer airports are based primarily on most recent actual data as reported to Airports Council International (ACI) through a survey. Future CPE information is available to the extent that airports publish future financial information in budgets, bond documents or other publications. This information has been compiled by a consultant. Future rates are generally not available. In 2015, the Port hired a consultant to derive future FIS rates for peer airports. Given the dearth of future rate information, staff has focused on changes to our own rates as in indication of problems and opportunities.

The 2015 Funding Motion requests annual updates for the following items:

- Projected final costs of IAF: still $608 million.
- Provisions of new airline lease agreement: current airline lease agreement runs through 2017, so no change at this time.
- Federal cap on PFCs: still $4.50, no change.
- Relative balance of international and domestic passengers at Sea-Tac: For 2015, international passengers accounted for 10.3% of total passengers.

ATTACHMENTS TO THIS BRIEFING

- Computer slide presentation.

PREVIOUS COMMISSION ACTIONS OR BRIEFINGS

- October 13, 2015 Aviation Division 2016 Budget Review briefing
- May 26, 2015 Commission Motion on Guidance for funding Airport Capital Improvement Program