PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA

Item No. 6b

Date of Meeting May 5, 2009

DATE: April 17, 2009

TO: Tay Yoshitani, Chief Executive Officer

FROM: David Soike, Deputy Director, Aviation
Kazue Ishiwata, Senior Marketing Manager, Aviation

SUBJECT: Authorization to implement a revised incentive program for new international air service with narrow-body aircraft, and improve facilities for Icelandair to begin operations at Seattle Tacoma International Airport (Airport).

ACTION REQUESTED

Request for Port Commission authorization for the Chief Executive Officer to: 1) implement a revised incentive program for new international, narrow-body commercial air service routes at a cost of $460,000; and 2), utilize Port staff and existing contracts to construct facility improvements at the Airport at a cost of $275,000 to enable Icelandair to initiate air service in July 2009. The total cost is $735,000.

SYNOPSIS

Icelandair recently announced they would begin direct passenger air service between Sea-Tac and Reykjavik, Iceland with beyond connections to Oslo, Stockholm, Copenhagen, Berlin, Munich, Barcelona, and other cities. The direct service between Sea-Tac and Reykjavik, an unserved destination, qualifies Icelandair to earn an incentive award from the Airport, under a revised incentive program for narrow-body aircraft. In addition, it is necessary for the Airport to make facility improvements to enable Icelandair to operate efficiently. Both the incentive and facility improvements are typical occurrences and has been provided for another airline that began similar new service to Mexico. The incentive program for Icelandair includes a one year temporary partial waiver of landing fees and arrivals charges. The Airport's joint marketing program funds would also apply to this new service. Facility improvements are always necessary when a new carrier arrives and begins new service at the airport. Facility improvements will be accomplished by Port Construction Services (PCS) crews, PCS existing on-call contracts, and by other Port in-house employees. The financial payback to the airport for all costs is estimated at less than 2 years.

BACKGROUND

Incentive awards for new service routes have been established at many large airports around the country. The Port Commission first approved the incentive program in December 2005. Incentive awards at Sea-Tac have been earned in recent years by Air France, AeroMexico, Lufthansa, and Hainan Airlines. All airlines require facility improvements in order to operate at an airport, and Sea-Tac is no exception.

SCOPE OF WORK

The scope of the revised incentive plan for use of a narrow body aircraft for this new route includes a temporary landing fee waiver of 75% of fees, and a temporary waiver of 75% of the international arrivals charge. Both waivers would extend for the first twelve months of operation. Under the revised incentive plan, Icelandair's new direct service qualifies to earn the same incentives approved by the Commission on April 10, 2007, for new service to Canada and Mexico.

In addition to the incentive plan, use of the long standing joint marketing program would also apply for the new passenger service. The initial support program would extend for the first three years of operation, which is a similar time frame applied to other prior new passenger service start-ups. These marketing funds are used to advertise and otherwise support the new Icelandair route during its infancy period in order to generate awareness about the route in the region to both the public and business marketplace. $110,000 will be applied in the first year, while $45,000 will be applied in the second and third year.

The facility improvements include modifying ticket counters, ticketing back walls, signage, communication/computer equipment, and gate hold room podiums/equipment at a total estimated cost of $275,000.

FINANCIAL IMPLICATIONS

Cost Estimate and Revenues

The total costs for the incentive program plus marketing program over the first year are estimated to be $370,000, while costs over the second and third year are estimated to be $45,000 per year. The total facility improvement costs are estimated to be $275,000 and would occur in the first year.

The total estimated revenues over the first year are estimated to be $351,000, while the revenues over the second year are estimated to be $674,000 and include landings, arrival charges, and other rents. It is anticipated that the payback period for the incentive program will be less than two years.

Source of Funds

Budget for prior incentive awards has come from either predetermined annual budgets when new service start-ups are known prior to the annual budgeting process, or from the Airport contingency when new start-ups are announced in the same calendar year they begin. The $110,000 joint marketing allowance will come from the contingency fund since the new service was just announced a month ago. Projected Cost per Enplanement (CPE) will not be affected since the contingency fund was included in the prior approved budget. The current lease agreement with the airlines provides for the airport to provide incentive program.

The budget for needed facility improvements will come from a combination of existing small capital or small jobs CIPs or contingency fund depending upon the type of work. This budget was included in the 2009 capital budget and plan of finance, and, as a result, the CPE will not be affected.

COMMUNITY / CUSTOMER / ORGANIZATION IMPACTS

Additional international air service provides new trade routes that spurs business opportunities and thereby strengthens and diversifies the local economy. Travelers enjoy a greater number of route options to match their needs and to help keep air service competitively priced. The airport benefits in the near term by increasing landing and arrival fees that help drive down average airline costs at the Airport.

PROJECT SCHEDULE

Facility improvements will be completed by late summer, incentive awards will extend for 12 months, while joint marketing allowances will extend for 36 months.

ALTERNATIVES CONSIDERED AND RECOMMENDED ACTION

Alternative 1

Do not provide an incentive award and do not improve facilities to allow Icelandair to operate at the airport. This alternative would not enable a new customer airline to begin service, and the airline would not be treated in an equitable manner similar to other airline customers.

Alternative 2

Provide an incentive award for direct passenger service to an unserved international destination by a narrow-body aircraft, and provide the necessary improvements to enable operations to be initiated in a smooth manner. **This is the recommended alternative.**

PREVIOUS COMMISSION ACTION

The Commission has authorized, was publicly briefed or notified regarding the incentive program in December 2005, in February 2007, in April 2007, and in November 2007.