The Airline-Airport Relationship

Objective: Review the main features of the relationship between airports and airlines; this relationship is sometimes synergistic and sometimes adversarial.

Outline

– Airport Use Agreements
– Role of airlines in airport governance
– Airport charges
– Sharing (or not) non-aeronautical revenues
– Provision of adequate capacity
– Cross-subsidies in multi-airport systems
– Ground handling
– Slots and access to markets
The relationship between airlines and airports is complex

On the one hand, it is highly synergistic; both wish to:

– Maximize passenger and cargo traffic
– Provide a high level of service (safe, secure, efficient, comfortable)
– Meet financial/business objectives

On the other hand, the airline is a “customer” of the airport, a relationship that often leads to conflicts regarding:

– Sizing of airport facilities
– Types of service and level of service provided
– Cost of use of the airport and size of charges for services
– Right of access to the airport when capacity is limited
– Equal treatment of all airlines

Lots of debate and controversy on some of these points
Keep in Mind...

- The relationship between airlines and airports varies enormously across countries and, in some cases, even across airports in the same country. 
  [We will present a range of current practices that illustrate this point.]

- The trend toward airport privatization has generally increased tensions in the relationship with airlines, as privatized airports are more motivated to focus on economic results.
The Airport Use Agreement

- This is a contract that the airline signs with the airport.
- Specifies the obligations of the airline and the airport during the period covered by the agreement.
- There is no standard agreement used internationally; major differences from country to country.
- Any major airline has to sign numerous airport use agreements (sometimes hundreds of them), one for each airport in which it operates.
- Agreements may concern:
  - large-scale operations at hub airports of the airline
  - a few daily operations at a peripheral airport
  - no operations (e.g., just having some office space at the airport)
Content of Use Agreements

- Specify the rights, privileges, and obligations of the airport operator and of the airlines

- Arrangements for access to facilities and costs to airline:
  - Premises and facilities leased and the degree of control by the lessee (e.g., exclusively leased, preferentially leased, leased in common, etc.)
  - Ticket counters, boarding gates, lounges, offices, etc.

- Rate-setting methodology used by the airport operator (e.g., residual or compensatory agreements in the US)

- Rights, if any, of airline to review and control expenses at the airport

- Other responsibilities and obligations of airport and airlines (insurance, indemnification, environmental issues, etc.)
Responsibilities of the Airline

- Payment of landing fees and security charges
- Collection of various airport related fees from passengers
  - “terminal use charges” at most airports,
  - various taxes and fees (e.g. ‘Passenger Facility Charge’ (PFC) in US)
- Maintenance and repair obligations (e.g., terminal complex, apron area, etc.)
- Make improvements to premises, under guidance from airport owner (often cost-shared)
- Provision of data (number of revenue and non-revenue passengers, connecting passengers, etc)
- Adherence to noise procedures
- Payment of property taxes
- Operational issues (gate scheduling, check-in counters)
Responsibilities of the Airport

q Airport must provide signatory airlines with:
   – Operational data
   – Financial data
   – Capital and operating plans
   – Right to audit airport finances

q Must operate the airport adhering to all applicable safety regulations

q Maintain adequate facility quality standards

q Carry adequate insurance

q Airport must show and adhere to its pricing methodology

q Provide any agreed ground handling services

q Provide any agreed fueling services
Additional Types of User Agreements

- Specific agreements for lease of space and facilities in the airport terminal
  - Office space
  - Space for VIP lounges
- Provisions for sublease of gates, ticket counters
- Land lease for:
  - Airline operations centers
  - Maintenance facilities
  - Cargo facilities
- Many other possibilities (North America, Munich)
Common Use vs. Dedicated Facilities

- Airport facilities and services may be”
  - “common use”
  - “dedicated” (or “exclusive”)
  - “preferred” (prioritization of use)

- Common-use facilities are typically developed by the airport operator, who also controls access by allocating gates and stands to airlines, with possible changes from day to day.

- Dedicated facilities may be developed by:
  - the airport operator and leased to specific airlines
  - jointly by an airline(s) and the airport operator
  - by an airline(s) under a BOT agreement

- Airport operator controls access to land parcels on airport property
The “Retail Park”

- 800 m² Food Plaza
- 500 m² Gas Station
- 10,000 m² DIY
- 26,000 m² Household
- 4,200 m² Electronics & Home appliances
- 12,000 m² Fashion Factory Outlet
Specific Important Points and Issues

- Role of airlines in airport governance and CAPEX decisions
- Charges for aeronautical services (landing fees, passenger terminal fees, security fees, etc.).
- Sharing, if any, of non-aeronautical revenues (from commercial activities at the airport)
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Role of Airlines in Airport Governance

- At practically every major airport:
  - Airlines form a committee of selected airline representatives (sometimes called “the IATA Committee)
  - Committee meets regularly with airport operator for updates on plans and to provide comments/feedback
  - True influence of these committees varies greatly

- But role of airlines in governance can be much stronger:
  - At many airports, one or a few dominant airlines exercise, in practice, great influence over the airport’s decisions, especially those involving large capital investments
  - In other cases (for example at many US airports), the use agreements may contain clauses that give airlines a major role in decision-making, especially concerning CAPEX (capital expenditures)
Example: US “Signatory Airlines”

- US airports rely heavily on bond issues to fund capital improvements.
- Some airlines sign long-term use agreements with these airports that the airport then uses to secure and obtain favorable financial terms for the bond issue.
- Essentially, these airlines guarantee payment of the bond.
- The airlines that sign such agreements are called “signatory airlines.”
- Any major capital expenditures by the airport must be approved by the majority of the signatory airlines under “Majority-In-Interest” (MII) clauses in the User Agreements.
- MII decisions may lead to disputes between airport operator and signatory airlines.
Concerns of Airlines re. Airport Planning

1. Unnecessary or excessive or misplaced capital expenditures (CAPEX)

2. Inadequate planning to anticipate, prepare and develop airport infrastructure to prevent severe congestion
   - Late realization of need to expand facilities

3. Failure to adopt a “systems approach” to planning
   - Example: increase size of terminal without increasing capacity of runway system

4. Insufficient consultation / coordination with airlines regarding infrastructure needs and investments

Source: IATA (2014) [Courtesy Dr. Sulmona]
Specific Important Points and Issues

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Procedure and decision-maker(s) for setting airport user charges also vary greatly:

1. Central government (usually with input from the airport operator and the airlines)
2. A “Regulator” (with input from stakeholders)
3. Regional or local government (with input from stakeholders)
4. Airport operator (with input from local airline committee, subject to approval by government or regulator)
5. Airport operator subject to approval by airline users (“majority-in-interest”)
Airport Charges Regulation in the US

- Publicly-owned airports – local and/or state government
- Aeronautical charges must be cost-related (essentially a “cost-plus” system, overseen by local authorities)
- Airports typically have long-term agreements with several airlines, which lease or co-own airport assets (terminal buildings, maintenance facilities, etc.)
  - For practical purposes, the charges are therefore largely pre-determined contractually
- Federal government may intervene when a potential violation of federal legislation is perceived
- Extensive and regular consultation with airlines re airport charges; majority-in-interest clauses in many cases
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Who benefits from non-aeronautical revenues?

- **A fundamental issue!** Becoming ever-more important as commercial revenues at airports keep growing.

- “Single till” vs. “dual till” controversy

- **Single till [supported by the airlines]**: Airlines are charged only for “residual” aeronautical costs, i.e., those not covered by non-aeronautical revenues

- **Dual till [supported by airport operators]**: Airlines pay aeronautical charges sufficient to cover the full cost of aeronautical facilities and services; non-aeronautical revenues are not considered

- **“Hybrid till” [compromise solution]**: An agreed X% of the cost of aeronautical facilities is covered by non-aeronautical revenues; the airlines are responsible for paying for the remaining (100-X)%. 

An Important Variation

- An important variation of single-till vs. dual-till is used in USA
- The residual cost system vs. the compensatory system
- Under “residual cost” (analogous to “single till”):
  - Airlines are charged only for residual aeronautical costs, i.e., the costs that remain after subtracting the airport’s revenues from non-aeronautical revenues
  - But, the airlines also sign use agreements under which they guarantee to cover airport debt in the event that the airport is unable to do so
  - The “signatory airlines” therefore assume a financial risk in exchange for sharing the benefits of non-aeronautical revenues

- The “compensatory system” is entirely analogous to “dual till”
In Summary...

- Under the “compensatory system” (=> “dual till”)
  - The airport assumes the financial risk of the operation
  - The airport keeps all the revenue from non-aeronautical activities
  - The airlines pay the full costs of the facilities they use

- Under the “residual system” airport and airlines share non-aeronautical revenues and financial risk

- 134 busiest airports in US: 22% Residual, 28% Compensatory, 50% Hybrid; 43% have majority-interest clauses
### Landing Fees*, Compensatory A/Ps, 2011

<table>
<thead>
<tr>
<th>Airport</th>
<th>Signatory airlines</th>
<th>Non-signatory airlines</th>
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<td>LGA**</td>
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* Per 1,000 lbs max landing weight, except 3 NY airports, where charge is based on maximum take-off weight

** Minimum: $100 at NY airports; $102 at LAX; $185 at SFO
## Landing Fees*, Residual A/Ps, 2011

<table>
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<th>Non-signatory airlines</th>
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<td>1.52</td>
</tr>
</tbody>
</table>

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Importance of Airport Capacity to Airlines

- Availability of capacity \(\Rightarrow\) operating performance of airline

- Limited capacity at an airline’s “hub” airport:
  - Limits airline connectivity (i.e., the ability to serve many markets, some at high frequency)
  - Increases operating costs (delay costs can be very high)
  - Reduces aircraft productivity (= fewer hours for flying)
    - forces increasing scheduled flight times to ensure on-time performance
    - *Note the undesirability of long taxi distances at airports* (Madrid, Amsterdam, Dallas/Ft. Worth)
  - Damages the image of the airline
Example of Congestion-Related Cost

- An airline schedules 200,000 movements per year at an airport where air traffic delays average 10 minutes per movement.
- Average cost to the airline per minute of aircraft delay is $80.
- Annual direct operating cost to the airline is \((200000 \times 10 \times 80 =)\) $160 million!
- Plus cost to passengers, plus negative perceptions about airline (although the airline is not responsible for the delays).
Specific Important Points and Issues

- Role of airlines in airport governance and CAPEX decisions
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- **Ground handling provisions**
- Cross subsidies among airports
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Ground Handling

- Provision of ground-handling services is an essential aspect of airport operations
  - Ramp handling, passenger handling, baggage handling, freight and mail handling, catering, (?) fueling
- Until late 1990s, many European airport operators retained monopoly rights over provision of ground handling services
- EU regulation on ground handling (1996):
  - At airports with more than 1 million pax, airlines have right to self-handle
  - At airports with more than 2.5 million pax, third party handling must be allowed and at least one handler must be independent of the airport operator or “dominant airlines”
- Slow implementation of EU regulation due to airport resistance
Ground Handling

- Ground handling can be provided by:
  1. The airport operator (or government agency)
  2. The airline itself ("self-handling")
  3. Another airline
  4. A specialized ground-service operator

- Airlines insist on at least two of 2, 3, and 4 being available and on the right to self-service

- Some airport operators still retain major involvement in all/some ground handling services

- Frequent cause for disputes or litigation
Specific Important Points and Issues

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Cross-Subsidies within a Group of Airports

- Many airport operators operate groups of airports (e.g., AENA 47 airports in Spain, BAA formerly 7 airports in UK, Port Authority of New York and New Jersey 6, Aeropuertos Argentina 33, etc)

- Some of the airports in group may be major international airports, while others are small domestic ones

- Airlines often concerned about cross-subsidies from the strong airports in group to economically weak ones

- Airport operators argue that such cross-subsidies strengthen the entire group of airports as a system

- National governments have often attempted to privatize airports as groups, so that weak airports can be privatized as part of a “package” that includes strong ones (e.g., Argentina, Greece, Mexico, Portugal, Spain)
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Importance of Airport Slots to Airlines

- Slot: A permission to use a runway and the airport’s infrastructure at a certain time
- At “Schedule Coordinated” (“Level 3”) airports, access to the airport is restricted to airlines that have been given slots
- Availability of slots → access to markets
- Historical holders of slots retain “Grandfather Rights” to these slots (subject to “use-it-or-lose-it” provisions)
- Unavailability of slots at desired times of the day may act to limit or distort competition at some Level 3 airports by keeping out “new entrants” – this may be true even in “Open Skies” environments
Diverging Positions on Market Access

- Approval of international routes: recent divergence between airlines and airport operators in North America and Western Europe

- Airports want to:
  - increase connectivity (number of destinations served)
  - tend to prefer long-range flights that use larger aircraft

- Therefore generally support liberal policies ("open skies") regarding approval of international routes

- New major carriers and new entrants are usually supported by airport operators when applying for routes to support open skies relationships

- BUT, some major North American and Western European carriers have been exercising pressure on their governments to adopt more protectionist route policies
### Emerging Carriers and Hubs

- **Emergences, Turkish, Etihad, Qatar**

**Annual airport passengers in millions:**

<table>
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<tr>
<th></th>
<th>2007</th>
<th>2014</th>
<th>% Δ</th>
<th>% Δ per yr</th>
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<tbody>
<tr>
<td>Dubai (DXB)</td>
<td>35</td>
<td>71</td>
<td>103</td>
<td>10.5</td>
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<td>57</td>
<td>148</td>
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<tr>
<td>Doha (DOH)</td>
<td>9</td>
<td>21*</td>
<td>133</td>
<td>18</td>
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<tr>
<td>Abu Dhabi (AUH)</td>
<td>7</td>
<td>20</td>
<td>186</td>
<td>16</td>
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</tbody>
</table>

* 2012 traffic

- Advantages: geographical position, aggressive carrier expansion, cost structure

- Fast growing share of traffic from Europe and America to/from Asia and Africa; Dubai now 2\textsuperscript{nd} most popular destination from LHR (after New York)!
References


q Slides 5-10 partly based on lecture by Dr. Michael Tretheway, InterVISTAS
Questions? Comments?