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WHAT CONSTITUTES EXCLUSIVE RIGHTS? OR HOW MANY FBOS ARE ENOUGH?

By The ABS Team

One of this month's "*Ask ABS*" question was related to the subject of exclusive rights. Carl Honaker, Director of the Santa Clara County Airports asked "How many FBOs are Enough...or too many?" If you ask the FAA this question, they might answer: "As long has your airport has land, every FBO operator has the right to lose money or even go bankrupt." Although this answer may seem humorous and capitalistic at the same time, it really doesn't answer the question.

It has become apparent recently that many airports and tenants have some serious misconceptions about what constitutes an "exclusive right" for FBOs at their airport. Most often, the airport's misconception starts with the concept that if you only have one FBO, you are granting that FBO the exclusive right to provide commercial aeronautical services at the airport. From the tenant's standpoint, the fact that they are, and have been, the only FBO provides them with some right to always be the sole provider. Both sides are equally misinformed.

The FAA provides some "details" on exclusive rights for which compliance is mandatory for airports that have accepted Federal assistance (although details from the FAA always have a tinge of "gray" in them). The statutory prohibition on exclusive rights currently states that "A person does not have an exclusive right to use an air navigation facility on which government money has been expended.", and an air navigation facility includes airports. However, they go on to clearly state that having a single fixed-base operator (FBO) is not always considered an exclusive right. Most commonly (and almost clearly) the FAA notes that if the airport sponsor can verify that it is unreasonably costly or impracticable for more than one FBO to provide aeronautical services, and/or when the existing FBO lease commenced prior to September 3, 1982, and the addition of a second FBO would require a reduction in the first FBO's leased space, having a single FBO would not be considered an exclusive right. However, there are numerous other scenarios where an airport can legitimately deny a second (or third, or fourth) FBO from commencing operations at the airport.

To provide additional insight, it is important to review some of the definitions that can sometimes get misstated or misunderstood. Here are the official FAA definition for several key terms used:

Exclusive Right – A power, privilege, or other right excluding or debarring another from enjoying or exercising a like power, privilege, or right. An exclusive right can be conferred either by express agreement, by the imposition of unreasonable standards or requirements or by any other means. Such a right conferred on one or more parties, but excluding others from enjoying or exercising a similar right or rights, would be an exclusive right.

Proprietary Exclusive – The owner of a public-use airport (public or private owner) may elect to provide any or all of the aeronautical services needed by the public at the airport. In fact, the statutory prohibition against exclusive rights does not apply to these owners and they may exercise but not grant the exclusive right to conduct any aeronautical activity. However, the sponsor that elects to engage in a proprietary right exclusive must use its own employees and resources to carry out its venture. An independent commercial enterprise that has been designated as agent of the owner may not exercise nor be granted an exclusive right.

The two most common issues which can be legitimate reasons for denying additional FBOs at an airport focus on financial viability and safety. As stated previously, the FAA's position is that "all operators have the right to go bankrupt"; however, the airport should insure that they, and their customers, are not impacted as a result. Some questions that should be asked by the airport are:

1) Is the recent growth in GA activity at the airport sustainable? (*Going from 300,000 gallons of retail fuel to 350,000 gallons in one year may be a 17% increase, but it is realistically only a 50,000 gallon increase. The same 50,000 gallon increase the next year is only a 14% increase, and the ratio will continue to decline.*)
2) Does the Airport benefit from an additional operator? *(Contrary to popular belief, doubling the number of FBOs does not double the fuel volumes or activity levels at the airport.)*
3) What happens with the facilities if one operator goes under? (*The airport may have to incur the maintenance responsibilities of vacated facilities which may or may not be functional for future replacement tenants.*)
4) What will be the long-term effect on the users of the airport with additional competition? (*Price wars may benefit the consumer in the short term, but cannot be maintained by two operators over the long-haul. Something has got to give, and customer service, amenities and safety are the first to be cut.*)

The FAA has stated on several occasions that the "economic hardship" argument only applies to the airport, and does not apply to the financial impact on incumbent FBOs on the airport. We respectfully disagree. The airport seldom has any "economic hardship" from allowing a second FBO, unless they are forced to expend money to accommodate the new tenant. Otherwise, under the worst case scenario, the airport gets additional ground rent and the same fuel flowage fees and percentage rents if the new entrant only results in the "splitting of the existing pie". It is our opinion that if the introduction of a new FBO creates a situation whereby both FBOs will realistically be unable to garner a reasonable return on investment, the airport and its customer will be the losers, and the airport has a responsibility to make sure that they are not facilitating the failure of one or more businesses. Putting an FBO into business to fail is not a prudent way manage an airport.

This is not to say that under no circumstances should additional FBOs be introduced to an airport. Sometimes competition is good, but at the same time, competition for competition's sake only is detrimental to everyone involved. Airports must make sure that new FBOs seeking entrance into the marketplace are fully informed as to the business environment at the airport, have a valid and economically viable business plan, and have the financial "where-with-all" to survive the lean years that will occur during start-up. A new entrant into the market that proposes to obtains 50% marketshare in Year 1 (or even Year 2) has probably not done their homework.

Obviously, Minimum Standards can be one of the most effective tools in dealing with the multiple FBO situation, and more importantly, avoiding the appearance of providing exclusive rights to an incumbent. However, like many other management documents, Minimum Standards are only valuable if the time, energy, and forethought was invested in their preparation. Careful consideration must be given to the ***minimum threshold requirements*** for becoming an FBO on your airport. While the FAA dictates that they must not be too restrictive as to eliminate qualified entrants, it is our opinion that they must not be so nominal as to provide for anyone with a

"doublewide and a fuel truck" can be granted a long-term lease and FBO operating agreement. Remember, it is your airport and as long as you can justify and support the reasons behind your decisions regarding Minimum Standards and other associated policies governing leasing standards at your airport, the FAA will usually support you. The FAA does not mandate that you have more than one FBO, nor do they imply that having one FBO dictates a monopoly. They are more concerned with an equal opportunity, as long as it does not impose on the safety of the airport.

In addition, as airport management tries to manage and maximize airport property, they should also consider whether or not to allow an existing FBO to respond to RFPs for new land leases if they have determined a need for competition (excluding the existing FBO is not a violation of the exclusive rights prohibition). Therefore, if you have an FBO with an existing lease and you are issuing an RFP for land to be used for a commercial aeronautical activity, you can legitimately exclude the incumbent from submitting a bid.

An airport operator can also deny a prospective business operator the right to engage in an on-airport aeronautical activity for reasons of safety and efficiency. The FAA encourages each airport operator to work with their local ADO or Regional Airports Office in determining whether or not safety would be compromised by the proposed aeronautical activity. Safety concerns are not limited to aeronautical issues, they may also include Occupational Safety and Health Administration (OSHA) standards, fire safety standards, building codes, or sanitation concerns.

Over the years, we have been asked "How many FBOs are too many?" many times. Unfortunately, there is no magic number or formula based on number of based aircraft or historical fuel sales. Each airport is unique and has different market demands that need to be analyzed. Competition is sometimes healthy; however, in many cases a single FBO can be the best alternative. Too many FBOs on an airport can saturate the market and lower service and safety levels. (As revenues decline, personnel costs move to the forefront, and line personnel turnover usually results. This creates an environment with new, untrained linemen that often infringes on a safe operating environment.) Alternatively, one poorly operated FBO that can easily run off both based and transient customers through a failure to focus on customer service.

In conclusion, the answer to "How many FBOs do you need?" is: IT DEPENDS! Every airport must carefully evaluate their market and make a determination of whether new entrants will potentially serve (realistic) "untapped" markets, or whether they are simply seeking to segregate the existing market. Pirating the existing market almost always results in the airport and its users being the losers over the long-term.

SUPER BOWL HIGHLIGHTS YOU WILL NOT READ IN *SPORTS ILLUSTRATED*

By Mark R. Davidson, A.A.E. Vice President

A couple of weeks ago, Jacksonville, Florida hosted Super Bowl XXXIX. As all the sport television networks mentioned time and time again, Jacksonville was the smallest city to host the "big game" in the history of the National Football League. Although the city was smaller than previous host cities, the question for us in the aviation industry is "How well did the system of airports perform in the Jacksonville region?" The following are highlights you will never read in *Sports Illustrated*, especially in their famous February issue.

To observe the activity, I made a field trip to Cecil Field, which was the primary general aviation facility during the Super Bowl. I state "primary" because the FAA allocated most of the slots to Cecil Field during the weekend of the event.

For those who are not familiar with Cecil Field, it used to be a Naval Master Air Base and contains three 8,000' runways, one 12,500' runway and 537,000 yards of apron space. In other words, "It's Huge!" During my visit on Friday before the game, sport celebrities such as Joe Montana and Magic Johnson utilized the Airport, and Signature Flight Support's offered a temporarily enlarged facility, complete with plasma screens and video games for the pilots. To entice potential buyers, Boeing even placed one of their new BBJs next to the terminal for travelers to tour.

Cecil Field had 120 aircraft on the ground the morning of the Super Bowl, and another 350 scheduled inbounds. One issue that caused some delays was that several of the inbounds dropped off passengers and then proceeded outbound. The increase in fractional ownership aircraft was apparent, and NetJets even had staff staged at the Airport. Cecil Field's Airport Manager, Rusty Chandler, informed me that around 12:30AM after the Super Bowl, the control tower had 92 jets in the queue, and they were departing every 45 seconds. Amazingly, the longest wait of the night was around an hour and half. In order to accommodate all of the parked jets, Rusty's staff closed portions of two runways which were west of the active runway the FAA was using. Not only did the closure provide additional space, it kept vehicle traffic from crossing the active runway. Due to the size of the Airport, the staff was able to direct each jet to a spot where the pilots were able to power in and power out. This minimized delays and potential liability that comes with towing and stacking aircraft.

The tower at Cecil Field is a contract tower, and the hours of operation were extended Thursday through Monday in order to handle the traffic. The Jacksonville Airport Authority paid for the additional hours and extra staff, while the FAA covered insurance after hours.

At the commercial airport on Monday after the game, Jacksonville International experienced approximately four times the number of people they usually process in a day. A temporary terminal was developed with the assistance of TSA to process the increased passenger flow. Once passengers were checked in, they were screened and bussed to their aircraft. The Jacksonville Airport Authority, as well as other GA airports in region such as Craig, Herlong, Fernandina Beach, and St. Augustine, had been planning for the event for four years, and it appears for all accounts that all the airports in the region performed well.

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Ask ABS!?!

In the past few issues, we have included a section called ***"Ask ABS"****, where we request aviation-related questions from our readership. Each month we publish one question from our readers with a reply from one of our professional consulting team. Even if your question is not selected, all questions submitted will be responded to via e-mail. Please submit your question to Mark Davidson at:* **mdavidson@airportbusiness.net**

Although Carl Honoker was the "big winner" this month, having his question answered with a full article, since we have a lot of white space left, we are going to address another question this month. Question No. 2 comes from Kenneth Maenpa, Assistant Airport Manager at the Jefferson County Airport outside of Denver, who asked several questions on the topic of leases:

Should an airport own facilities or improvements, and what about resulting competition with private enterprise? Also, how and should we deal with lease term extensions from existing tenants? Should term extensions include the extension of the reversion of improvements? What about capital improvement requirements? Is there a standard matrix ratio between capital improvement investments and the number of years of a lease?

The decision of whether an airport should build improvements is generally an economic one relative to the ability to generate the capital necessary to construct improvements, and priorities of allocating capital to tenant-based projects as opposed to more widely beneficial ones. The "ownership" of leasehold improvements is usually an issue of control. As such, it is my opinion that if the airport has the ability to finance leasehold improvements, this is usually the best option. This scenario usually provides for the greatest control and leverage over a tenant, as well as the ability to generate significant revenues for the airport. Not only can the airport usually lease the facilities for more than their debt service on the new construction, but future rent increases will provide additional revenue opportunities. While the tenant will likely want the ability to depreciate the improvements, the up-front costs will provide the tenant with capital to invest in other aspects of the business.

Regarding lease extensions, it depends upon the tenant and their history at the airport. If you have a tenant that has diligently performed under the terms of their lease, and is willing to invest in the operation going forward, then "Why not?". (This assumes that there are not other prospective and qualified parties that may have solicited the airport.) However, it is important to treat an extension just like any new lease. Negotiate investment criteria, lease obligations, reversion clauses, and other terms from a position of strength. If existing improvements are scheduled to revert at the end of the existing lease, rent for the improvements should begin at the scheduled point in the new lease (at prevailing market rental rates), or overall rent should be adjusted to reflect the fact that the airport would be entitled to improvement rent at the end of the existing lease. Always remember that a lease extension is a privilege, so the tenant must "give something to get something."

Finally, regarding the relationship between term and capital investment, unfortunately, there is not a uniform policy in the industry in this area. It can significantly vary depending upon the region of the country and local economics, as well as the real needs of the tenant and airport. The key is to make sure that the investment requirement enhances the value of the facilities to provide for greater value at the time of eventual reversion.

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