

## Airport Financing on a Shoestring Budget: An Analysis of LOI Funding To Date

By Carrie Farley

FAA's current reauthorization act expires in September 2007, requiring Congress to revisit FAA funding at a time when airport capital improvement programs are requiring substantial expenditures. In the past, these expenditures were funded almost entirely by Airport Improvement Program (AIP) grants. Due in part to increasing capital improvement costs, AIP funds in many cases are no longer able to fully fund large programs. Given the current constraints under which the AIP operates, the president's DOT budget request for fiscal year 2007, which includes a proposed cut of almost \$800 million in AIP funding, has raised additional concerns about future funding levels. While the funding for these grants has been growing at about 3 percent per year in nominal terms, the president's proposal would cut AIP by over 20 percent (See chart below).

for their capital improvement programs. Additional funding is being found through innovative financing solutions, such as Passenger Facility Charge (PFC)-backed bonds or the use of State Infrastructure Bank (SIB) loans. FAA has helped to make financing these projects easier by working with airports to guarantee funding levels for many multi-year projects through Letters of Intent (LOIs). Financial markets have welcomed this step as additional assurance that FAA funds will be forthcoming, reducing some concerns about the availability of future funding. Given the increasing reliance on financing plans that require guaranteed funding sources like the LOI, understanding how LOI grants have been used in the past becomes particularly important.

projects have ranged greatly in the amount of funding provided and the LOI length. In terms of length, there appears to be a preference for five- and ten-year LOIs. When examined based on the value of LOIs issued, the preference for ten-year LOIs is particularly pronounced (see Fig.1 and 2). Roughly one-third of the funds committed through LOIs were committed over a 10-year term, and just shy of two thirds of these funds were committed in LOIs of between five and ten years in length.

The FAA also appears to favor funding levels below \$40 million, with more than 60 percent of the LOIs issued under this threshold (See Fig. 4). FAA has issued LOIs up to \$337 million (for the Chicago-O'Hare Modernization Program), with a total of four LOIs in excess of \$250 million. However, only 8 percent of the LOIs issued were for more than \$150 million. The preference for lower-valued LOIs may be a reflection of the relatively few projects that have funding requirements in excess of certain levels. It does seem, though, that FAA is willing to fund large portions of large projects.

### Size and Length of LOIs

Since 1990, the FAA has committed almost \$5 billion through 83 LOIs to a variety of projects that, per AIP funding guidelines, focus on capacity, safety, security and noise reduction. These

AIP Funding	
Fiscal Year	Amount (billions)
2000	\$1.90
2001	\$3.20
2002	\$3.30
2003	\$3.40
2004	\$3.40
2005	\$3.50
2006	\$3.40
2007	\$2.75

With growing capacity needs and the likelihood that substantial increases in funding from Congress won't be forthcoming, AIP funding may continue to become further constrained.

As a result of these constraints, airports are increasingly relying on AIP grants as only a portion of the funding

Fig.1 LOI LENGTH BY NUMBER OF LOIS

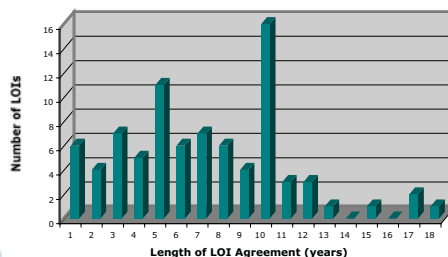
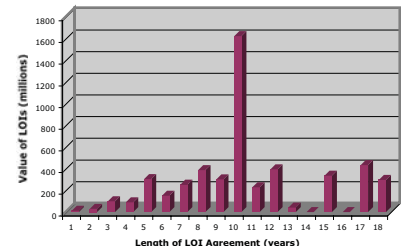
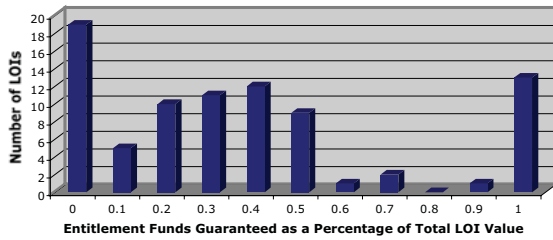


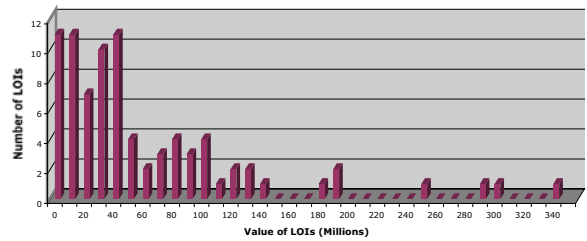
Fig.2 LOI LENGTH BY LOI VALUE



**Fig. 3** COMPOSITION OF LOI VALUE ENTITLEMENT VS. DISCRETIONARY FUNDS



**Fig. 4** LOI AMOUNT



### Committal of Entitlements

AIP entitlement funds are determined based on the passenger traffic at an airport; in a given year, enplanement data from two years prior is used to calculate the exact value of entitlements for that year. This lag is to enable the airport to predict the entitlements that it will receive in future years; however, this does mean that the airport will not know what it will receive more than two years in advance. The LOI program was created as a way to reduce the uncertainty surrounding these fluctuating entitlement funds. Therefore, it required that all entitlement funds be pledged to the proposed project.

Based on the LOIs issued to date, however, these entitlement funds may or may not be guaranteed as part of the total value of the LOI. In fact, most LOIs guarantee more discretionary funds than entitlement funds (see Fig. 4). Particularly notable is that almost 23 percent of LOIs guaranteed only discretionary funds. Thus the LOI application process is not merely a way to secure future forecasted income, but to apply for and secure AIP discretionary funding. Moreover, in the 23 percent of projects with no guaranteed entitlement funding, entitlement uncertainty was not mitigated, and may still be a concern from the perspective of the project to which these funds are pledged.

### Airport Size

A final piece of information examined relates to the funding that is available to airports of different sizes, as meas-

ured by enplanements. In 2004, large hub airports comprised two percent of airports eligible for AIP funding, yet carried 70 percent of the passengers that flowed through these same airports. In terms of LOI funding, large hubs received 35 percent of the LOIs issued, and 60 percent of the funding committed through LOIs. Airports in the Other category, comprised of non-hub, non-primary and GA airports which are eligible for AIP funding, received only 6 percent of total funding, and 18 percent of the LOIs issued. These same airports comprised 93 percent of those eligible for AIP funding yet served only three percent of the passengers that flowed through eligible airports.


While large hub airports receive the bulk of LOI funding, their share is still somewhat less than the percentage of passengers they serve. However, the smallest airports, those in the Other category, receive twice the amount of funding as their share of passenger traffic would indicate. This disproportion may be due, to some extent, to the fact that many smaller airports are unable to access funding through financial markets; and, that the continued existence of smaller airports benefits all the users of the wider air transportation network.

An analysis of LOI funding over the last 15 years indicates a few trends:

- The length of LOIs tends to be between five and ten years;
- The value of an LOI is rarely more than \$150 million, and tends to be less than \$40 million;
- Entitlement funding may or may

not be included in the funds guaranteed by an LOI; and

- LOI funding is primarily towards large hub airports. However, the smallest airports are still receiving substantial funding in relation to the proportion of passengers they serve.

While the items above serve as general guidelines, what is most interesting to emerge from this analysis is the flexibility of the LOI program. LOIs have funded very large and very small projects. LOI funds have been committed for as long as 18 years and as short as one year. LOI commitments have been comprised entirely of discretionary funds, entirely of entitlement funds, and a range in between. In short, the FAA seems very willing to tailor this tool to a variety of different projects. This flexibility is very important as funds become more constrained, as it enables FAA to leverage the utility of its authorized discretionary funds in the hopes of achieving its goal of a safer, more efficient air transportation network. 

*How does this experience compare to your airport? If you would like to share your ideas and information, please e-mail [cfarley@imggroup.com](mailto:cfarley@imggroup.com).*

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