38TH ANNUAL AIRPORT LAW WORKSHOP

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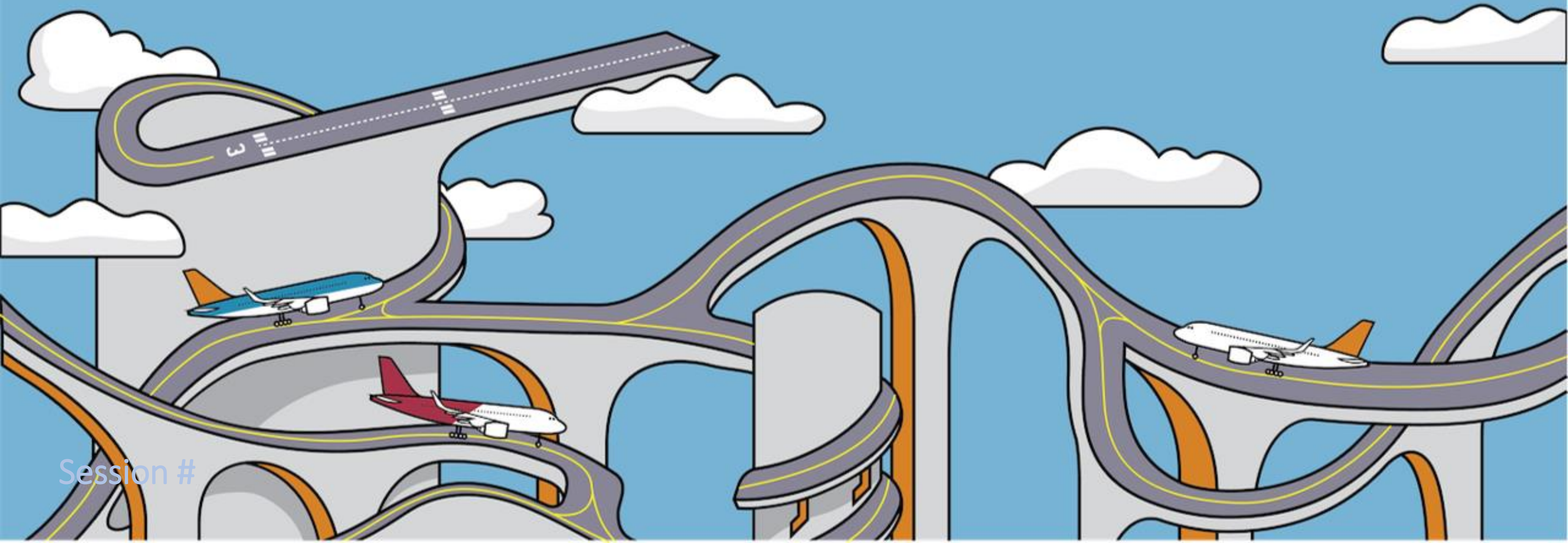

Session #

Advanced Topics in Airport Finance

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Our agenda

- Examine airport finance in terms of project delivery
- Multiple sources of funding, and multiple sets of requirements
- Deeper dives into debt financing and private sector delivery
- Putting it all together – establishing a comprehensive program of finance
- Q & A

Project delivery

- Breaking large projects into multiple sub-projects –consider many factors, including the financial plan
- Fund projects with separate sources of funding
- Matching funds to projects is an art and a science!
- Legal requirements can guide means of project delivery – FOLLOW the MONEY!
- Financial plan is key, but don't lose sight of risk management, project management, phasing, etc.

Project funding vs. financing

- Funding and financing are not the same
- Project funding does not require repayment
- Financing is borrowed money
- All airport projects require funding, not all require financing
- It is often practically difficult or financially unwise to avoid financing
- Financing depends on funding
- Available funding may not be able to support desired types of financing

Multiple sources of funds; multiple requirements

- Airports rely on multiple sources of funds for capital projects
- Each funding source has its own requirements and restrictions
- Break larger projects into subprojects that can be funded separately
- How will proposed project provide a financial return?
- Develop a funding model

AIP requirements and restrictions

- See AIP Handbook, FAA Order 5100.38D for eligibility guidance
- Costs funded with AIP cannot be included in rate base
- AIP typically used for projects not leased to airlines or others
- When applied to eligible project costs, can be means to reduce rates and charges
- Distinguish apportionment and discretionary grants

PFC requirements and restrictions

- See FAA Order 5500.1 for guidance on project eligibility
- PFC-funded costs cannot be included in the rate base
- PFCs treated as “local” funds; can be local match
- PFC project eligibility slightly broader than AIP; falls into 3 broad categories
- Gates funded with PFCs may not be subject to long term, exclusive leases
- Requires extensive consultation process with airlines and FAA approval

Use of airport revenue

- Most flexible source of funds; can be used for any airport purpose
- May be restricted by other agreements: e.g., AULA, Indenture
- May be recovered from users, depending upon provisions of relevant agreement(s)

Airport Revenue Bonds (GARBOs?)

Bond basics

- Bonds are a loan – a promise to pay from specified revenues
  - Pledge of funds
  - Single borrower, generally multiple lenders
  - Trustee = lenders' representative
- Airport bonds = revenue bonds
- GARBs vs. special facilities bonds
- State law governs bond issuance
- Federal law controls federal tax exemption
- Federal securities laws govern disclosure

Bond funded projects

- May be used for any airport (or non-airport) purpose
- Best to finance revenue-generating projects
- The legal trifecta of bonds:
  - If tax exempt, will require in-depth tax analysis and compliance
  - Public offering will trigger federal disclosure obligations under securities laws
  - Issuance requires compliance with statutory requirements

Why bonds?

- Bonds allow for asset/liability matching
  - Repayment terms matched to the assets' lives
  - Users pay the capital cost as they use them
- With tax exemption, provides low cost of capital
- The market – including rating agencies, investors, SEC and IRS – monitors financial management and long-term focus

The Bond Indenture / Trust Agreement

- A critical airport agreement – you need to know it!
- Pledge: specified revenues
  - What revenues are pledged or excluded?
  - How are PFCs treated…what about federal COVID-19 relief grants?
  - What flexibility is provided?
  - Interaction with use and lease agreement
- Covenants, e.g.,
  - Coverage tests
  - Additional bond tests
  - Maintenance of assets
- Additional bonds test
- Restrictions on amendment

TIFIA for airports

- A new flavor of debt – TIFIA recently extended to airports
- A loan from US DOT
- Deeply subordinated (but must be investment grade)
- May defer all payments until project is in operation
- Interest rate tied to federal rates
- Complex application and approval process

Federal securities laws

- What is a “security”?
- SEC’s limited power to regulate municipal bonds
- Rule 10b-5
  - Materiality
  - Responsibilities of issuers and others
  - Applies to all statements to “the Market”
- Rule 15c2-12
  - Primary disclosure – the Official Statement
  - Secondary disclosure
    - Annual filings
    - Event filings

Key credit considerations

- Size and strength of local market – “catchment area”
- Importance of reserves – days cash on hand
- Strength of management
- Response to and recovery from COVID-19 pandemic
- Legal provisions
  - Flow of funds – priority of debt service
  - Required debt service coverage
  - Application of PFCs and other funds
  - Covenants for benefit of bondholders
  - Other security (e.g., airline step-up in ULA)

Private Development – Not a Panacea, but an Opportunity

Private development characteristics

- Structuring typically is bespoke – no “off the rack” deals
- Identification and allocation of risks is a hallmark
- Investors / partners expect a return – typically higher than bond rates, although less assured
- Often ideal for a unique or unfamiliar facility or project
- Private development: more than financial expertise or resources – project delivery, not just financing

Breaking down financing options for private development

- Equity – distinctions in perspectives and expectations by type of investor (not all investors or private partners are alike)
- Debt – commercial loans, private placements, taxable / tax-exempt bonds, federal and state loans
- TIFIA for airports
- In each case, account for the context

Defining private development

- Includes an array of project delivery arrangements, traditional and novel
- The hallmark – private developer takes economic risk due to project outcomes – how risk is transferred can vary
- Common opportunities for private development include:
    - Private airport development
    - Airport privatizations
    - Long-term lease, concession, operations, license or similar arrangements
    - Design-build-finance (DBF) through design-build-finance-operate-maintain (DBFOM)
    - Development rights in exchange for infrastructure
- **Start by structuring the project, not by conforming the project to a structure**

Laying the groundwork for private development

- Partnering with the private sector is a means to an end – focus on what you are trying to accomplish, and then work to ‘how’
- First identify your goals, funding opportunities and constraints: does private development makes sense?
- Private development is neither a panacea nor a source of free money

Laying the groundwork for private development

- Permits financial innovation and structures that increase the value of funds
- Can pair financing methods with project delivery and management approaches
- Common approaches to repayment:
  - Direct access to revenues – most often at risk
  - Payments for performance (“availability payments”)
  - Access to PFCs, grants and other sources
  - Management or other traditional fees for services
- Not all private partners can work with all payment models – model chosen must be ‘bankable’

Walking through private development scenarios

- So you want to…
  - Build a new terminal or introduce commercial air service?
  - Build a ConRAC?
  - Transfer & leverage parking operations & revenues?
  - Transfer airside management
  - Develop new airside facilities?
  - Reimagine your cargo facilities?
  - Provide innovative means of access?

Putting it all together

- There are multiple sources of funds and financing – what is best for you?
- Understand your project(s) and your airport
- Start by structuring the project – not the financing
- Address legal constraints of funding and delivery up front – know the limitations and benefits of the various methods

QUESTIONS?