MARKET ANALYSIS
**an editorial opinion**

# Can FBOs remain competitive in their local markets? How will the actions of airport sponsors affect the industry?

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These are challenging times for our industry, and how we proceed will define where we are headed in the future. I believe that maintaining an ongoing dialogue that addresses the issues we face is integral to achieving our collective success.

We continue to find ourselves reacting to industry events as they unfold—and, indeed, after they have unfolded—rather than preparing for and confronting them in advance. I am of the opinion that we need to steer our own destiny or we will find ourselves in the position of having little or no future choices other than those that we have allowed to evolve.

I myself prefer "driving" as opposed to simply "going along for the ride," so I make sure to tell my industry brethren to keep their "eyes wide open and their hands on the wheel" by being proactive rather than reactive. I suggest that as an industry we start looking ahead, for I fear that we are headed down a road that presents tremendous risks to our financial viability.

## Airport sponsors and their evolving industry role

The airport sponsor is actually the owner and operator of a given airport. Since airport funding comes from the federal government (ie, FAA) and the state (ie, DOT), the airport sponsor ends up being the local municipality—county, city or both—which operates the airport through these funds.

Airport sponsors accept funds under the terms and conditions of the federal, state and local jurisdiction's guidelines. Additional revenue sources are generated through rent from tenant leases and user fees that include fuel flow and landing fees. Airport sponsors play a significant role in their FBO tenants' pricing structure for services that are charged to the airport's flightline consumers. They do so by the manner in which they structure and administer FBO lease agreements and impose fees. Recent trends in this regard are having a profound effect on the pricing consumers experience for aviation services at airports around the nation. The result is a mixed bag that represents "the good, the bad and the ugly." I will discuss these effects in greater detail below, but without naming specific airports or service providers.

Perspectives vary according to one's role in the industry (eg, airport sponsor, FBO tenant or airport user/consumer).

Panorama Flight Service was host of the 2011 NBAA Northeast Regional Forum held at HPN (White Plains NY). It will host next year's event on Jun 6, 2013. (Inset) Panorama Pres Gene Condreras.

**Showalter Flying Service at ORL (Exec, Orlando FL).**

In addition, short and long-term effects of our collective actions must be considered thoroughly while looking at a series of very complex issues that are driving industry action and the motivation behind them.

## Airport sponsor-owned FBOs' proprietary right

FAA notes in Advisory Circular (AC) 150/5190-6 that most airport sponsors recognize that aeronautical services are best provided by profit-motivated private enterprises. However, there may be other situations—such as when revenue potential is insufficient to attract private enterprise and the airport sponsor wishes to exercise its proprietary right to be the exclusive provider of any or all aeronautical services at the airport. The sponsor of a federally obligated airport is the only entity entitled to hold an exclusive right to perform aeronautical services. For the sponsor to exercise this right, commercial aeronautical services must be performed by the sponsor's employees, using the sponsor's own equipment and resources. A sponsor may not grant an exclusive right to perform these services to any other individual or entity.

And therein lies what may be considered a very vague and gray area. How is it determined that the revenue potential at a given airport is not sufficient to attract private enterprise? And who makes this determination?

Once an FBO has been established as an airport-sponsored proprietary right FBO, does the airport give up its right—and the subsequent revenue—associated with being the sole service provider, as overall airport traffic volume and sales grow over time? Having looked at a number of airports around the country where this has occurred, I have to say no—it does not.

One could make the argument that there is a trend in numerous areas of government whereby government looks for additional revenue sources, instead of looking to improve services. Under these circumstances, government is in a unique—and unfair—position to create its own monopoly by structuring contracts to suit its own needs. Is it not possible that the airport sponsor might issue an RFP that makes no business sense in order to justify implementation of an airport-sponsored proprietary right FBO?

Over the years, airport-sponsored proprietary right FBOs have gained a generalized reputation for charging on the high side of market scale while providing inferior services and value to their customers. Since they provide the only services available at their airport, there's little or nothing the airport user can do other than avoid the airport and take its business elsewhere if there happens to be a convenient alternative that fits their travel mission profile.

Recently, a certain airport-sponsored proprietary right FBO in a busy and popular business aviation market area has made a name for itself by providing exceptional facilities, service and pricing to the users of their airport. Aviation consumers are very pleased, as is the airport sponsor, and it would seem that everyone is happy. Everyone, that is, except for the competition located at nearby airports that compete for the same consumers' business. These competitors question whether perhaps the airport-sponsored proprietary right FBO is factoring capital improvement costs as a line item when formulating its consumer pricing and reviewing its subsequent profits and losses. From the consumer perspective this is of little concern—after all, pricing, service and facilities are their criteria, their focal point for comparison.

Only time will tell how these competing FBOs in the surrounding market area will be affected, and whether future changes of general manager at the airport-sponsored proprietary right FBO or changes in the local political landscape that dictate the airport's financial protocol will have any bearing on consumer value received at this location. At present, this is one of the very few airport-sponsored proprietary right FBO success stories in the US that GA and corporate aircraft consumers speak about.

## Airport sponsor-owned FBOs that compete with FBO tenants

AC 150/5190-6 also states that an airport sponsor may contract the management of an airport sponsor-owned FBO to a management agent. If the sponsor uses such an agent, that agent becomes the de facto airport sponsor and must abide by all grant assurances—with the exception that the agent does not possess any proprietary right to provide services, and must allow competing service providers that meet the minimum standards to operate. In the event that the airport sponsor decides to provide an aeronautical service in direct competition with a tenant service provider, the airport sponsor must meet the same minimum standards as other similarly situated service providers.

The problem is that an FBO tenant cannot effectively compete with its landlord, especially when the landlord is the airport sponsor. When airports use federal and state grants to build hangars, and then set prices below those needed to recover the cost of construction of such infrastructure, it makes it impossible for private industry to compete. In certain cases, this may be considered to rise to the level of an "unlawful taking" in that an airport sponsor has the ability to push well established and competitive FBOs out and away from a location, thus leaving themselves to set all the rules and service standards for the traveling public using the airport.

In a letter dated Aug 6, 2012 addressed to FAA Acting Administrator Michael Huerta, 12 members of the US House of Representatives expressed a concern that "there is a recent trend of airport-sponsored fixed based operations (FBOs) competing with privately-owned FBOs". The members state that "[they] are concerned that airport-sponsored FBOs, whose budgets are supplemented by federal funding, have a competitive advantage stemming from these taxpayer subsidies when compared to private-

| Description | CT | NJ | NY |
|---|---|---|---|
| **Federal and state fees (cents per gallon)** | | | |
| Federal excise tax | $0.2430 | $0.2430 | $0.2430 |
| LUST tax | $0.0010 | $0.0010 | $0.0010 |
| NJ gross receipts | | $0.0400 | |
| NJ jet aircraft fuel tax | | $0.0200 | |
| NY petroleum business tax | | | $0.0710 |
| **Total federal/state taxes (cpg)** | **$0.2440** | **$0.3040** | **$0.3150** |
| **Airport specific fees** | | | |
| Airport storage fee | | $0.1600 | |
| Airport flow fee | $0.05 | $0.0400 | $0.1650 |
| **Total airport specific fees** | **$0.0500** | **$0.2000** | **$0.1650** |
| **State percentage fees** | | | |
| Connecticut gross receipts tax rate | 7.000% | | |
| Average fee at time of writing | $0.2546 | | |
| New York State sales tax rate | | | 7.3750% |
| Average fee at time of writing | | | $0.4100 |
| **Total state percentage fees** | **$0.2546** | **$——** | **$0.4100** |
| **Total price per gallon** | **$0.5486** | **$0.5040** | **$0.8900** |

**Sample tax and fee structures of 3 similarly situated airports in the NYC metro area that compete for the same customer base of business.**

ly-held FBOs. Therefore, [they] request that FAA provide guidance to ensure that Grant Assurance 22 (economic nondiscrimination) is properly enforced so that all FBOs, both privately and publicly owned, compete on a level playing field."

There has been a lot of aviation press concerning an airport at which a privately-owned FBO weathered a rocky economy and managed to sustain financial viability in the wake of what I believe was 2 former competing FBOs closing up shop and ceasing operations. The city decided that it was in consumers' best interests to use state airport grants funded from aviation fuel taxes to build new FBO facilities at the airport. Once it had built these beautiful new facilities, the airport contracted with a small, reputable, well-known FBO chain to manage the airport-sponsored FBO.

The aforementioned letter to FAA Acting Administrator Huerta from the US House of Representatives makes specific reference to this airport and to the current situation, stating that "recent evidence from the 'airport' proves that airport-sponsored FBOs do not operate efficiently and require unnecessary and costly taxpayer support. The city reported losses of $317,000, which was $200,000 more than anticipated. Since airport-sponsored FBOs do not have a profit motivation, capital losses do not present a fundamental problem. However, these losses are passed on and result in wasted taxpayer dollars. Such scenarios can be avoided by the use of privately-owned FBOs [which] do not rely on taxpayer subsidies and must operate within a budget."

The CEO of said airport maintains that, although it is true that the new FBO has lost more money in its first 11 months of operation than originally anticipated, this is "because competition is working." He further states that "fuel prices at the airport have dropped so remarkably that the primary source of revenue for the 2 FBOs has also dropped."

I believe that this statement warrants careful consideration. One must ask oneself whether this really means that the reduced margins that the airport-sponsored FBO established—and that the existing FBO was forced to compete against—led to a financial loss because the reduced margins were not enough to sustain financial viability. It may also be worth asking the following questions. What will happen when or if the privately-owned FBO closes its operations at the airport and goes out of business because it can no longer sustain the losses caused by operating with reduced margins? Will the airport terminate its contract with the FBO chain that was managing its FBO's day-to-day operations and exercise its proprietary right to be the exclusive provider? In the event that it does not, will any other privately-owned FBO want to execute a lease and compete with its landlord? Once the airport-sponsored FBO is the only FBO on the airport, will it then set margins back to a level that will properly cover the costs of providing service? Will the users of the airport actually benefit in the long term if the airport-sponsored FBO is the only FBO doing business at the airport?

The airport's CEO claims that "the temporary loss is covered by significantly increased net operating revenues in other areas of the airport, and is a small price to pay for saving corporate pilots, general aviators, airlines and cargo carriers an estimated $1.5 million in the first year alone." He also states that the airport built the new FBO facilities with state airport grants funded solely from aviation fuel taxes, not through general taxpayer funds. In other words, only those who bought aviation fuel in the state paid for it.

Some may find it ironic that the FBO forced to compete against its landlord collected a portion of the aforementioned taxes from the fuel that they'd pumped as an airport tenant, only to have those taxes used at a later date to build the airport-sponsored FBO facility that now competes against it. I believe that the airport CEO's statement that "the temporary loss is covered by significantly increased net operating revenues in other areas of the airport" has to be alarming to anyone who currently operates a privately-owned FBO.

The letter from the US House of Representatives to FAA may be expressing this very concern when it states, "We believe the temptation for the airport sponsors to advance their own business interests, with the aid of taxpayer subsidies, to the detriment of privately-owned FBOs, may lead to abuse and unnecessary waste of increasingly limited taxpayer dollars. Therefore, we respectfully request that the FAA put controls in place to ensure that conflicts do not arise when airport sponsors assume the dual role of regulator and competitor."

Just such a case may occur should an airport sponsor, as regulator, demand leasehold renovations on the private FBO's facility but not allow for an adequate term of the lease to provide an opportunity to achieve a return on investment.

It is reasonable to assume that, at the aforementioned airport, taxpayer dollars are now being used in order for


Banyan Air Service at FXE (Exec, Fort Lauderdale FL).


Clay Lacy Aviation VNY (Van Nuys CA).

the airport-sponsored FBO to be able to continue to operate at a loss. This leaves the privately-owned FBO at a tremendous disadvantage. Aviation has been built on the application and execution of safe and professional service standards. To ensure the proper and consistent implementation of both those principles I believe it requires investment of capital and reinvestment of profits. Competition in aviation should be motivated by increasing safe and professional services to users of an airport—or it should be market-based, depending on the demand needed to support those profit-driven services. Gauging the success of competition in a given market by basing it on the decrease in average fuel price to the consumer falls far short of the mark when it comes to the criteria needed for intelligent consideration of how the airport's actions will affect its users in both the near and long term.

## Airport sponsor practices, imposed taxes and fees

Are private FBOs placed at a disadvantage when the airport sponsor deems that non-FBO tenants have the right to store and dispense their own fuel? Are they placed at a disadvantage when the airport sponsor allows non-FBO tenants to sublet their facilities or portions of their facilities to other non-FBO tenants? And do the aforementioned practices diminish revenue-generating sources for their FBO tenants?

The taxes and fees that an airport sponsor imposes on the airport's users and tenants has a direct effect on the cost of services that consumers pay at a given airport location. For example, the New York metropolitan market has a significant number of airports in close proximity to one another. They are located in 3 different states (New York, New Jersey and Connecticut) and all are competing for the Manhattan private aviation consumer market.

It's worth noting that New York's aviation fuel tax structure is significantly higher than that of New Jersey and Connecticut. As of Aug 22, 2012, based on current market cost and pricing, the tax on jet fuel (either direct to the consumer or included as part of the FBO's cost) in New York was 42.10¢ per gallon higher than in New Jersey and 22.64¢ per gallon higher than in Connecticut. (New York's taxes are based on a percentage of the retail sale price of the fuel, while Connecticut's taxes are based on the wholesale cost and New Jersey's are fixed.)

A New York FBO must decide whether to lower its margin to compensate for the reduced taxes in the neighboring states, thus allowing it to remain competitive with those FBOs. Airport-specific fuel flow fees charged by the airport sponsor can further increase the gap between pricing to the consumer, depending on the airport's geographical location and fee structure.

Airport sponsor lease agreements with their FBO tenants also have a profound effect on pricing to the aviation consumer. For example, many airports around the country require that a fuel flow fee be paid directly to the airport sponsor. Further, some airport sponsors also require that a ramp fee and possibly landing fees be paid. As a matter of practicality as well as reality, the fees that an airport sponsor charges its tenants and users of the airport have a direct effect on its FBO tenants' ability to be competitive with other airports and FBOs in the surrounding area. Let's face it. Pricing differences of up to \$2.00 a gallon at airports just 34 nm (about 10 min) apart—because \$1.80 of that difference is being paid directly to the airport sponsor in the higher-priced market—will surely drive a significant amount of business away from the higher-priced airport and its FBO tenant. The same holds true with regard to ramp and landing fee mandates that result in significant pricing differentials between area airports. Again, an FBO tenant must decide whether to pass these costs along to the consumer in its pricing or remove them from its margin in order to remain competitive.

## Aviation consumer perception

We are often told that consumer perception is the same as reality when it comes to business. Why is this? Because the consumer's perception becomes its own personal reality and often cannot be changed by a third party. As an FBO business owner—and someone who is genuinely passionate about the industry and concerned with where we're headed in the future—I asked more than 700 business associates from my contacts database 2 questions to help me gauge their perception of airport sponsors and their evolving influences on our industry.

I asked them, "Is it the industry's perception that an airport authority's ownership of an FBO ultimately raises or lowers the cost of services to the consumer in the long term?" I also asked, "Does the industry realize that the state and local tax structure, fuel flow fees and ground rents at a given airport have a direct effect on that airport and its tenants to compete effectively with the surrounding airports located within relatively close proximity?"

I received 35 detailed responses. Most were from other FBO owners and FBO general managers whose opinions


Pentastar PTK (Pontiac MI).


Texas Jet at FTW (Meacham, Fort Worth TX).

were pretty close to those of my own. It was the flightline consumers' responses that truly surprised me—not so much because they were not in favor of single-FBO airport locations but instead always favored competition, but because they were so dead set against government's involvement and influence on our industry. Let me summarize with my 2 favorite responses.

The first is regarding airport sponsor-owned FBOs. "My flight department flies in excess of 450 hrs per year in an all-Part-91 environment. We are a national company with over 600 locations in 47 states, so we fly to all airports large and small, privately run [airports] as well as those regulated by the airport authority. Any time an airport authority gets involved with regulating how and where FBOs do their business we as customers suffer greatly."

The other refers to the effects of airport sponsors' taxes and fees. "I have seen several very competitively run FBOs in very busy airports lose control of their bottom line. Our flight departments are forced to find alternative airports and/or our uplifts are drastically reduced. This creates a snowball effect. The airport authority sees lower revenue streams due to decreased traffic and fuel uplifts. This produces the need to raise pricing, flowage fees and taxes, thus creating a continued cycle and the slow destruction of the businesses and the airport."

## What is to be done

As I stated earlier, we need to encourage discussion and share our opinions with the airport sponsors at the airports where we're based as well as at the airports that we frequent, and see where it goes.

A dear friend of mine offers the following analogy for consideration. He says, "I like to compare the stability of our industry to a 4-legged table. The 1st leg is the airport sponsor. The 2nd is the FBO or aviation service business with leasehold interests to provide services. The 3rd leg is the vendors that support the FBO [by providing] fuel, insurance, equipment, training, etc. The 4th or last leg is the aircraft operator, pilot or consumer who supports the FBO. If any one of these legs becomes broken or wobbly, the table is unstable."

Let's do our best to ensure the stability of all 4 legs. One possible solution for maintaining a stable industry is requiring a respectful partnership between those 4 legs that strengthen the table.

It starts at the local level. Former Republican President Ronald Reagan and then Speaker of the House "Tip" O'Neill—a Democrat—were known to sit down together after a day's work to enjoy an adult beverage. Both men were leaders because of their strong but differing principles. They were respectful of their duties to represent the people and were respectful on a personal level to enjoy one another's friendship and insights when the day's work was done. This respect and friendship carried over into their professional careers to establish them as leaders of the people they represented—and often allowed them to work in a bipartisan manner while representing their respective parties and the people of the United States.

Speaker O'Neill is quoted as saying, "All politics is local." Local implies sitting down from time to time to understand—and care—about what's going on in our aviation community. We need to discuss openly our collective goals and challenges with our state and local government officials, our airport managers, colleagues who may also happen to be our competitors, FBO business owners, local pilots and the transient aircraft operators that use our airports.

All politics is local, and the way to provide a vibrant market for aviation services at city, county and state level is for private and public enterprise partners to work together to provide the highest standards for safe, professional services. In order to do this we must understand and respect each other's different roles as well as those of airport sponsors, profit-motivated aviation business and service providers and airport users themselves. If we do this, we may achieve the aviation community's collective goals for our airports. And if doing this helps at even 1 airport then I believe it was a worthwhile endeavor.

Increased communication leads to thorough consideration of the effects of airport fee structures and how they relate to an airport's ability to be competitive.

In addition, we must not lose focus on maintaining the airport consumer's ability to operate within a financially viable budget.

I always say that you never know how much of an impact you can make until you try. Most readers know by now that I enjoy trying. Call, write, communicate and play a significant role in creating a respectful partnership between our 4 major industry components. Long-term success will result from a collective effort that best serves all who have a vested interest in attaining this goal.

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