

**Federal Aviation Administration Airport
Financial Compliance Review of the
Memphis-Shelby County Airport Authority**

Conducted March 13 – 24, 2017



Memphis-Shelby County Airport Authority Federal Aviation Administration Airport Review

The Federal Aviation Administration (FAA) Office of Airport Compliance and Management Analysis (ACO) conducted a compliance review of the Memphis-Shelby County Airport Authority (Authority) to evaluate compliance with Airport Improvement Program (AIP) grant assurances and the FAA Policy and Procedures Concerning the Use of Airport Revenue (Revenue Use Policy) for the period July 1, 2011 to June 30, 2016. The FAA conducted this review at the Administrative Offices in the Memphis International Airport, Memphis, Tennessee on March 13 through March 24, 2017.

Authority Background:

The Authority owns and operates the Memphis International Airport (MEM), General DeWitt Spain Airport (M01), and the Charles W. Baker Airport (2M8). MEM is a small hub airport with 2,016,089 enplanements¹ in calendar year 2016. Enplanements declined 50% in fiscal 2013 from a peak of 5.56 million in fiscal 2008 due to the reduction of service with Delta Airlines termination of hub services². MEM benefited by becoming a 100 percent origin and destination traffic based airport; increased competition with moderate air carrier diversification; and MEM is experiencing a growth in enplanements of 10.7 percent since CY 2014. The Authority's finance staff worked diligently to sustain a solid financial base. MEM retired almost \$300 million in long-term debt over the last 11 years and maintains strong credit ratings from Moody's Investor Service (A3/Stable0 and Standard and Poor's (A-/Stable). (See Fitch's news release <https://www.fitchratings.com/site/pr/1028941>). MEM operates two Fixed Based Operators (FBO) at the airport (Wilson Air Center and Signature Flight Support).

MEM is the principal hub for Federal Express Corporation's package delivery operations and ranks as the world's busiest cargo airport with more than 30 million square feet leased on airport property. Federal Express accounts for the majority of MEM's total landed weight with the cargo operations. Federal Express Corporation's headquarters are located at MEM.

¹ Final CY 2016 Passenger Boarding Data, Enplanements at All Airports (Primary, Non-primary Commercial Service, and General Aviation) by State and Airport, FAA website https://www.faa.gov/airports/planning_capacity/passenger_allcargo_stats/passenger/.

² Ibid.



General Aviation Airports

General DeWitt Spain Airport (M01) and Charles W. Baker Airport (2M8) are classified as General Aviation (GA) airports. M01 is located five miles northwest of the central business district of the City of Memphis. The Authority manages the airport's FBO. Services at M01 includes extensive aircraft maintenance, flight school with pilot training from private pilot to flight instructor, aircraft rental,

hangar and T-hangar rental and helicopter services. M01 does not have a control tower, but MEM provides radar service to pilots operating out of the airport. Charles W. Baker Airport (2M8) is a Federal surplus GA airport located 10 miles from the central business district of Memphis, Tennessee. Services at 2M8 includes an FBO selling fuel, rental car agency and charter service (no regular service is provided).

Since FY 1982, the Authority has received approximately \$675 Million in AIP grants. Airport sponsors agree to certain obligations when they accept either federal financial assistances or federal property conveyances. The FAA enforces these obligations through its Airport Compliance Program. Unlawful revenue diversion is the use of airport revenue for purposes other than the capital or operating costs of the airport, the local airport system, or other local facilities owned or operated by the airport owner or operator and directly and substantially related to air transportation or property. The Office of Compliance and Management Analysis has the responsibility to ensure airports adhere to this policy. The Office of Compliance conducts a financial compliance review of several airports each fiscal year. These reviews disclose the airports' adherence to FAA grant assurances and the Revenue Use Policy.

Our compliance review of the Authority's airports included:

- Form 126 & 127 Reporting;
- Marketing, Promotion, and Air Carrier Incentives;
- Police Services;
- Aircraft Rescue and Fire Fighting Services;
- Leases and Uses of Airport Property;

- Legal and Lobbying Services;
- Financial transactions between the airport and other government entities; and
- Noise Land.

In this report, we address the FAA's findings and concerns about the use of airport revenues. Accordingly, the FAA requests the Authority, as airport sponsor, to provide additional information or submit a corrective action plan to the FAA's concerns. The federal statute of limitation is 6 years, so the corrective action plan will include the period of July 1, 2011 to June 30, 2016.

Review and Analysis

FAA Form 126 and 127 Operating and Financial Summaries

The Authority prepares the FAA Form 126 and 127, Operating and Financial Summaries for MEM. On the Form 127, the Authority reports selected balance sheet, income statement, and certain statistical data relevant to airport operations. The FAA requested the Authority prepare a reconciliation of selected amounts reported on Forms 126 and 127 to the Airports' Comprehensive Annual Financial Report (CAFR) and other supporting documentation.

FAA Conclusion: FAA found no issues with the reports.

Transactions between Authority and Other Governments

In addition, to relying on the independent audit report, we also tested several transactions between the Authority and surrounding governments to determine if the airport supported those transactions with journal entries and detailed invoices.

FAA Conclusion: Based on our review of direct charges between the Authority and the surrounding governments, we found the Authority complies with the Revenue Use Policy.



Marketing, Promotion, and Air Carrier Incentives

The Public Information Office has numerous marketing projects in progress to promote existing services. An air-carrier incentive program is in place to bring new service to MEM with assistance provided for airline marketing. The airport spent \$263,000 in FY 2014, \$311,000 in 2015, and \$643,000 in FY 2016 for marketing and promotions. The marketing is for promotion of the airport only; airport marketing expenses cannot support the general economic development or tourism in Memphis and the surrounding area. The Authority has contracted with Red Rover, a public relations firm to present the airport in a positive perception to the public. Red Rover services include web page updates, an increase in the use of Google and social media, videos for commercials and promotion, newsletters. Red Rover provides support and counsel to marketing.

The Authority hosts an annual golf tournament benefitting the Oakhaven Elementary, Middle and High Schools located in Shelby County, TN. The FAA considers expenditures that are “directly and substantially related to the operation of the airport” as standard if the contribution has the intangible benefit of enhancing the airport’s acceptance in local communities impacted by the airport. (See Revenue Use Policy, 7704). The FAA does not have an issue with hosting the golf tournament event.

The Authority provides monthly bus tours of Memphis for new airport employees. The FAA questioned the attendance of tenant employees and were informed that the attendance by tenants was minimal. Due to materiality, the FAA has no issue at this time but we encourage the MEM to monitor this going forward.

Air-carrier incentives are the same for all carriers. None of the air carriers is receiving subsidy payment. The air-carrier incentives are limited to a two-year limit. Incentives are not included in the airport's rates and charges. The Authority does have a list of desired routes to be promoted. The FAA did find payments to Allegiant Airlines for co-operative marketing. After analysis, we found the airport was paying their percentage of target marketing directly to the airline. We requested the Authority make their payments directly to the marketing firm and not to the airline. The Authority has taken corrective action.

The Authority does provide an information booth at MEM to the traveling public. Volunteers staff the booth at no cost to the airport.

FAA Conclusion: FAA found the marketing co-payment to an airline as questionable, but our analysis did not determine anything indicating improper use of airport funds. The Authority corrected the issue promptly. The Authority will make separate payments to the marketing firm providing marketing services in the future. No other issues.

Police Services



The Memphis International Airport Police Department (MAPD) is an airport department not affiliated with the Memphis Police Department or the Shelby County Sheriff's office. The MAPD does have a mutual aid agreement with Memphis Police Department and the City of Memphis EMTs in case of a major on-airport emergency. MAPD's jurisdiction is over all airport properties, tenant properties (including FedEx and UPS facilities) and outlying airport grounds. Staffing consists of 51 commissioned Law Enforcement Officers (LEO), 12 Traffic Enforcement Officers and 16 motor units, with separate divisions for investigations of incidents and airport patrol. The department utilizes 4 K-9 units to help protect the airport property, staff and airport patrons.

The ID Office of MAPD is responsible for dispatch services and badging for airport access. The ID Office processes all airport access requests with the assistance of background checks prepared by the Federal Bureau of Investigation (FBI).

MAPD does not respond to off-airport police calls unless the emergency calls are within their mutual aid agreement. The airport provides special security details for VIPs on an as needed basis. All arrests are transported to the Shelby County Sheriff's Office for booking. There are three shifts of 8.5-hour shifts for the terminals' patrols. Overtime policy is in place and monitored.

FAA Conclusion: FAA found no issues with Police Services.

Aircraft Rescue and Fire Fighting



Aircraft Rescue and Fire Fighting (ARFF) involves the response, hazard mitigation, and rescue, if necessary, of aircraft passengers and crew involved in an airport ground emergency. The department's services are

contracted through the City of Memphis Division of Fire Services. The City of Memphis' (City) Fire Station 33 is located on the airport providing structural fire services in conjunction with ARFF Station 9 providing aircraft fire and rescue services on the airport. Station 33 is not dedicated to the airport providing firefighting/EMS services to the surrounding community. The City does not pay any rent to the airport for Station 33. We will address this issue in the following Leases and Use of Airport Property section of this report. There are mutual aid agreements in place with the City.

ARFF is staffed with 23 positions working three 24-hour shifts. If any of the ARFF staff are absent, they can be backfilled from the Part 139 qualified staff at Station 33. ARFF has three specialized vehicles on site of Station 9, and a fully equipped Advance Life Support (ALS) paramedic ambulance stationed at Station 33.

FAA Conclusion: FAA has no issues with ARFF services, but we will discuss further use of airport property by the City without paying FMV rental fees for Station 33 below in our report.

Leases and Uses of Airport Property



Each federally assisted airport owner/operator is required by statute and grant assurances to have an airport fee and rental structure that will make the airport as self-sustaining as possible. These fees minimize the airport's reliance on Federal funds and local tax revenues. Aeronautical user charges however are subject to the standard of reasonableness and nondiscrimination, but they may be set at less than FMV. The FAA has generally

interpreted the self-sustaining assurance to require airport sponsors to charge fair market value (FMV) commercial rates for non-aeronautical uses of airport property depending on the airport's circumstances.

During our review, we were informed of the following about airport leases:

- The Authority approves all leases with no influence from other entities;
- All lessor constructed facilities revert back to the airport;
- There is no community use (e.g. soccer fields, recreational parks, running/bicycle trails) of airport property; and
- No through the fence (TTF) access to the airport.

Questionable Leases and Terms

In our review, we found most commercial and T-Hangar leases did not contain escalation clauses or rent adjustments. In some cases, lease agreements had not been adjusted for almost twelve years. Lease agreements should have an escalation clause requiring:

- Adjustment of the rental fees according to the Bureau of Labor Statistics Consumer Price Index for All Urban Consumers (CPI-U) periodically. The FAA recommends periodic adjustment at a minimum of five-year increments of the lease agreement.
- Adjustment of long-term lease agreements based on a periodic appraisal of the property. We recommend the appraisal be prepared at least every five-years.
- The escalation clauses should be included in new lease agreements or extended lease agreements.

Fire Station 33

The Memphis Fire Services (MFS) has a structural fire-fighting station located on 4.126 Acres of airport property. The City built the facility for structural firefighting and the support of the ARFF operations on airport property. The Authority and MFS have a memorandum of agreement (MOA) for the fire services provided to the airport. Fire Station 33 does not have an aeronautical mission on the airport requiring the City to pay FMV for the occupied property. However, the Revenue Use Policy does allow rental payments offset to reflect the value of services actually provided to the airport by the fire-fighting units. (See Revenue Use Policy, 7721, E.2).

The FAA requested the Authority to provide the type and amounts of in-kind services that Station 33 is providing the airport, which are not included in the MOA. These in-kind costs cannot be charged directly or indirectly to the

Authority to qualify as an offset. The MOA between MFS and the Authority lists the personnel and operational expenditures that the Authority is responsible for reimbursement. MFS personnel services that are part of the MOA reimbursement would not be considered as in-kind services. In FY 2016, the Authority paid the City \$3,501,524 for fire/EMT services. The Finance Department has provided a schedule of Station 33 costs versus in-kind services and benefits provided. We will be requesting clarification of the schedules.

FAA Conclusion: FAA recommends MEM to update lease agreements, whenever possible, to include provisions for adjustments to CPI-U periodically. Property should be re-appraised periodically or at least every five to eight years.

Fire Station 33 in-kind expenses to offset rental fees are still under negotiation.

Noise Mitigation

Aircraft noise affects the surrounding communities abutting the airport. Noise mitigation efforts have been implemented with the development of regulations. Title 14 Code of Federal Regulations (C.F.R.) Part 150 (October 25, 2004) was enacted to reduce the noise levels created by aircraft utilizing the airport. Noise programs may be funded with Airport Improvement Program (AIP) grants, and airport revenues may be used to mitigate aircraft noise on or off the airport.³ MEM does have a Title 14 C.F.R. Part 150 noise mitigation agreement approved and signed with the FAA. The noise program has been self-sustaining for sixteen years using the proceeds from the noise land's sale funds. MEM does provide noise complaint outreach for the community. MEM staff informed us that the airport only received nine complaints in FY 2016.

FAA Conclusion: MEM and the Authority comply with FAA Policy concerning noise mitigation.

Recommendations:

1. **Marketing and Air Carrier Incentives** - FAA found the marketing co-payment to an airline as questionable, but our analysis did not determine anything indicating improper use of airport funds. MEM corrected the issue promptly. The airport should continue making separate payments to the marketing firm providing marketing services in the future.
2. **Leases and Use of Airport Property** - FAA found in most commercial and T-Hangar leases that there were no escalation clauses or rent

³ Title 49 U.S.C. §§ 47107(b) & 47133

adjustments. Lease agreement contracts must have an escalation clause requiring:

- Rental fee adjustments according to the Bureau of Labor Statistics Consumer Price Index for All Urban Consumers (CPI-U) periodically. The FAA recommends adjustment at least each five-year increment of the lease agreement.
- Adjust long-term lease agreements based on a periodic appraisal of the property. We recommend the appraisal be prepared at least every five to eight years.
- The escalation clauses should be included in new lease agreements or extended lease agreements.
- **Fire Station 33** – The City of Memphis (City) Department of Fire Services provides structural firefighting and Aircraft Rescue and Fire-Fighting (ARFF) services based on a memorandum of agreement (MOA). Fire Stations 33 (structural fire services) and 9 (ARFF) are located on airport property. Fire Station 33 is not dedicated to the airport providing structural firefighting services to MEM and surrounding residential and commercial areas. The City should be paying FMV rental for the use of airport property. The City requests to offset these FMV rental fees with the cost of in-kind services, which are not a part of the MOA provided to the Authority. Negotiations are continuing concerning the determination of the offset expenses versus the rental fees.

Corrective Action Plan

Please prepare a corrective action plan that resolves the findings and recommendations presented in this report. The plan may include rebuttals to the findings and recommendations, and may include additional information the FAA may not have taken into consideration in its findings. Please provide a response within 60 days.