



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: John Aitken

**SUBJECT: PUBLIC HEARING FOR COVID
RECOVERY AIRLINE SUPPORT**

DATE: July 28, 2020

Approved

Date

7/28/2020

REPLACEMENT

REASON FOR REPLACEMENT

Two specific items are herein added to the original Council Memo for August 4, 2020:

- 1) Extension of the fee waiver period for intercontinental (non-North America) flights from June 30, 2021 to June 30, 2022 in order to recognize the specific challenges of a timely reinstatement of long-haul service. Many nations are still under quarantine conditions and other travel restrictions that continue to delay the return of international travel demand, and U.S. designated gateway airports including those in San Francisco, Los Angeles, and Seattle are likely to be deemed highest priorities for initial service.
- 2) Hainan Airlines has been added to the list of qualifying international carriers that were serving Norman Y. Mineta San José International Airport (SJC) prior to the global COVID-19 impact. Although Hainan notified SJC officials of permanent suspension of passenger flights, the airline has since been operating all-cargo aircraft into the Airport and could conceivably consider its own reinstatement of service. For that reason, Hainan would also qualify for fee waivers under this proposal.

RECOMMENDATION

- (a) Conduct a Public Hearing pursuant to California Government Code Section 53083 regarding support for the resumption of international flights by Air Canada, Alaska Airlines, ANA, British Airways, Hainan Airlines, Southwest Airlines, and Volaris Airlines as authorized by the Federal Aviation Administration.

- (b) Adopt a resolution authorizing the Director of Aviation or the Director's designee to provide support in the form of fee waivers for the air carrier services outlined in the table below:

Airline:	Air Canada	Alaska Airlines	ANA Airways	British Airways	Southwest Airlines	Volaris Airlines	Hainan Airlines
Routes:	Vancouver	Guadalajara San Jose del Cabo	Tokyo	London	San Jose del Cabo	Guadalajara Leon Morelia Zacatecas	Beijing
Frequency	3 Daily	3 Daily	1 Daily	1 Daily	1 Daily or Less	3 Daily	4/week
Support Period	3 Months	3 Months	6 Months	6 Months	3 Months	3 Months	6 months
Landing Fee	(\$88,354)	(\$173,296)	(\$333,336)	(\$333,336)	(\$7,238)	(\$171,184)	(\$190,478)
Waivers							
FIS Fee Waivers	n/a	(\$438,307)	(\$352,944)	(\$354,586)	(\$16,768)	(\$440,770)	(\$272,037)

For each route, landing fees and FIS (international arrivals) fees are waived as estimated for the respective qualifying periods.

OUTCOME

Norman Y. Mineta San José International Airport (SJC)'s tremendous growth over the past several years has clearly outpaced the industry as a whole, with calendar year 2020 holding promise for another record-breaking year that would have surpassed the milestone of 16 million total passengers. However, the global outbreak of COVID-19 has had massive world-wide impact and has virtually grounded a very large portion of the commercial aviation industry.

Given the severity of these unprecedented circumstances, increased competition for air service by carriers that are systematically downsizing their aircraft fleets, and the high costs of operating commercial flights, the Airport seeks to take a proactive partnership role through temporary, limited-term fee waivers specifically targeting the return of all of the important international routes that have been suspended as a result of the pandemic. Not coincidentally, British Airways and Volaris are already actively engaging airports on the specifics of any potential partnership support.

The table below shows the estimated total fees that would be waived if pre-COVID levels of international service were reinstated. Although it is difficult to project the outlook for passenger volumes and their spending behaviors, it is reasonable to believe that there will also be rising levels of other revenues from these flights from the return of concessions, parking, Passenger

Facility Charges (PFCs), and other activities. As in normal times, the positive revenue impact from these sources are projected to outweigh fee waivers; without these flights, the landing and FIS fees would not be generated at all.

Air Canada, Alaska, ANA, British Airways, Southwest, Volaris, Hainan Routes							
Airline:	Air Canada	Alaska Airlines	ANA Airways	British Airways	Southwest Airlines	Volaris Airlines	Hainan Airlines
Routes:	Vancouver	Guadalajara San Jose del Cabo	Tokyo	London	San Jose del Cabo	Guadalajara Leon Morelia Zacatecas	Beijing
Total Airport Fees and Net Psgr Spend	\$696,166	\$1,075,625	\$1,286,129	\$1,289,053	\$37,170	\$1,340,827	\$927,965
Total Waivers	(\$88,354)	(\$611,603)	(\$686,280)	(\$687,922)	(\$24,006)	(\$611,953)	(\$462,514)
Net Impact	\$607,812	\$464,022	\$599,849	\$601,131	\$13,164	\$728,874	\$465,451

After the expiration of the support periods, long term revenues associated with these routes will continue to benefit the financial situation of the Airport for continued years of service. To avoid the waivers of these fees impacting other carriers serving the Airport, funds from the Coronavirus Aid, Relief, and Economic Security Act (CARES) grant to SJC may be proposed in a future budget action, if necessary, to offset waiver amounts.

BACKGROUND

The Airport is a strategic asset for achieving the City's economic development goals. Air service provides an essential link to support and sustain Silicon Valley's quality of life by moving people and products between San José and both domestic and global destinations. Gaining better access to national and international markets and technology centers has long been a priority of the region's businesses. Community and business leaders and travelers have clearly expressed their strong desire to the Airport for improved access between San José and key domestic and international cities.

The Airport continues to maintain a formal Air Service Support Program that has continued to evolve since its introduction in 2006. The SJC program, similar to those that are widely used across the industry, remains consistent with the Federal Aviation Administration's policies, and is designed to offer support for NEW commercial airline service. The Mayor and City Council have been consistently and unanimously supportive of this program, having seen the net positive

revenue and economic impact benefits of new service that helped achieve SJC's record setting pace over the last several years.

Today, however, the COVID impact is rapidly changing the landscape for commercial airline service around the globe. While acknowledging the importance of SJC's domestic route system to our Silicon Valley market, this initiative is specifically focused on the international services that serve global travel needs of our residents and visitors alike. For several reasons, the uncertainty of the return of international flights remains a major concern:

- International flight operations tend to be more complex and costly, with governmental approvals required and the expense of wide body aircraft operations needed for intercontinental routes;
- Other communities aggressively compete for international service as a visual confirmation of their ties to the global marketplace;
- At this time, the return of service to London, Beijing, Tokyo, and several Mexico routes continues to experience postponements;
- International airlines are beginning to actively solicit actions to reduce airport costs as part of their route reinstatement decisions, including British Airways (issuing formal Requests for Information from all of its 26 North American Airports) and Volaris (similarly but less formally engaging SJC and 20 others in the U.S.);
- Competitive pressure from SFO has grown significantly, with international air service capacity that has increased 52% over the last five years;
- Evidence of the potential loss of international service as has already been witnessed by our other Bay Area neighbor, Oakland International Airport;
- Uneven levels of worldwide government support for their country's respective airlines places additional pressure on the prospects of reinstating international air service.

For these reasons, the Airport is taking a strong approach to communicate our partnership commitment to the seven commercial airlines that have provided unique international services to serve the business and personal international travel needs of our community.

ANALYSIS

International airline service to SJC has remained a high priority to the City and stakeholders across the Silicon Valley market being served. The waiver of fees is already a key element of our program that targets new and expanded service, and is welcomed by our commercial airlines as a partnership mechanism to help offset initial operating costs during a period in which the route performance hasn't reached maturity.

In all of the international routes being presented in this memo, the combination of non-waived airport fees and estimated passenger impact through Passenger Facility Charges (PFCs), rental car fees, Commercial Facility Charges (CFSs), airport concessions, and airport parking outweighs all waivers.

Although the waiver of fees is no guarantee that a route will be reinstated or return to a sustainable level of profitability, such waivers are within the Airport's abilities to encourage the return of international flights. This same analysis has been shared with Council for every new route that has been presented, resulting in unanimous support and final approval.

Recommended Support

The seven airlines outlined in this memo and the destinations that they have served confirm SJC's commercial links to the global economy. Recognizing that the Airport is not the primary international hub of the Bay Area, it remains important to maintain these services and continue to develop those that are competitive, serve the needs of our region, and consistent with the City's Economic Development strategies. As noted, funds from the CARES grant to SJC may be proposed in a future budget action, if necessary, to offset waiver amounts. Council support for these international routes is recommended.

Air Canada, Alaska, ANA, British Airways, Southwest, Volaris, Hainan Routes

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Landing fees and FIS fees are waived at 100% for the duration stated for each qualifying route, and will be continually monitored by members of SJC staff.

CONCLUSION

Norman Y. Mineta San José International Airport has dramatically increased its ability to serve the City's business and leisure travelers through several consecutive years of record-breaking air service expansion. Unfortunately, the outbreak and impact of the COVID-19 virus dramatically altered the entire global commercial aviation industry, leading to border closures, quarantines,

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aircraft groundings, and a number of policy decisions that virtually shut down the vast majority of international travel.

Locally, this situation also led to a derailing of SJC's continued record-setting trajectory, leading to the same 90% or greater passenger reductions seen across the nation compared to 2019. As of this writing, domestic flights and passengers are showing signs of modest rebounds, but the same cannot be said for international routes.

Under these circumstances, the Airport proposes taking a proactive partnership lead targeting the reinstatement of international flights that were fully operating prior to the virus outbreak. As is true with our support program for new service, the proposed fee waiver plan for returning international service is consistent with Federal Aviation Administration's policy, is not a subsidy to any airline, and remains revenue positive during temporary fee waiver periods due to the ongoing collection of non-waived fees such as office rents, baggage space rents, and other exclusive use space rents and net fees generated by passenger activity at the Airport.

As noted throughout this memo, each of the routes represented in this memo generate net positive results to the Airport and to the City in excess of the values of landing fee waivers:

Air Canada, Alaska, ANA, British Airways, Southwest, Volaris, Hainan Routes

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Net Impact	\$607,812	\$464,022	\$599,849	\$601,131	\$13,164	\$728,874	\$465,451
Annual Economic Impact Estimates	\$4,946,033	\$19,647,241	\$103,918,756	\$103,918,756	\$357,434	\$20,156,611	\$79,726,030

Although the waivers to be offered by SJC cannot guarantee each airline's profitability on reinstated flights due to many financial and competitive factors, the City's Council's endorsement of this plan and its application to the airlines presented in this memo clearly reflects a commitment to serving the needs of our community.

EVALUATION AND FOLLOW-UP

Airport staff will monitor the return of flights to the specified destinations supported by the fee waivers to ensure that adherence to the program specifications is maintained throughout the application period.

CLIMATE SMART SAN JOSE

The recommendation in this memo aligns with one or more Climate Smart San Jose energy, water, or mobility goals.

POLICY ALTERNATIVES

Alternative #1: The City Council may choose not to approve the proposal for support to assist in the reinstatement of international airline services as outlined in this memo.

Pros: None.

Cons: If Council does not approve application of this proposal, chances of the reinstatement of international flights will be put in jeopardy. The airlines might choose not to operate the service altogether, as other airports become better options for the allocation of aircraft. The fee waiver proposal is designed to help encourage the return of SJC's international services following the COVID-related suspension and ultimately to benefit the Airport and the City.

Reason for not recommending: International air service carries a high profile and speaks to the City's global reach, providing a strong balance to the Airport's largely domestic route network. Failure to offer support during the periods of service re-entry creates additional barriers to reinstatement and would signal to our airlines that the City and SJC are not proactive partners fostering expansion. Without these international services, SJC's revenue growth would be jeopardized and the economic impacts to the community would not take place.

PUBLIC OUTREACH

This memorandum will be posted on both the Airport's website and on the City's Council Agenda website for the August 4, 2020 Council meeting. The August 4, 2020 Council meeting will serve as the economic development subsidy public hearing in amounts in excess of \$100,000, as required pursuant to California Government Code Section 53083 and as further described in the Fiscal/Policy Alignment discussion below.

COORDINATION

This memorandum was coordinated with the City Attorney's Office and the City Manager's Budget Office.

COMMISSION RECOMMENDATION/INPUT

This item does not have explicit input from the Airport Commission, although Commission members are provided with regular updates of airline services and proposed program changes and have expressed support of the Airport's Air Service Support Program and the use of fee waivers as a viable partnership approach.

FISCAL/POLICY ALIGNMENT

This project aligns with the City's Economic Development Strategy #9 "Keep Developing a Competitive, World Class Airport, and Attract New Air Service."

Application of fee waivers to assist the air carriers in succeeding financially in reinstatement of international destinations will benefit the City. The Office of Economic Development's financial multipliers were used to calculate the following City-wide economic impact statistics:

Air Canada, Alaska, ANA, British Airways, Southwest, Volaris, Hainan Routes

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COST SUMMARY/IMPLICATIONS

Funding from the CARES grant to SJC may be proposed in a future budget action, if necessary, to offset waiver amounts, estimated to be \$3,172,631, if all international flights are reinstated to pre-suspension levels. Increased revenues from non-waived fees, Passenger Facility Charges, airport parking, concessions, car rentals, Customer Facility Charges, and other sources are projected to offset landing and FIS waivers. Additionally, the wider economic impact for the City resulting from the reinstatement of these flights has been exhibited in this document.

The table below again summarizes the total net fees and revenues to the Airport compared to the combination of landing fee and FIS waivers provided to support the re-entry of service.

Air Canada, Alaska, ANA, British Airways, Southwest, Volaris, Hainan Routes

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CEQA

Not a project, File No. PP17-003, Agreements/Contracts (New or Amended) resulting in no physical changes to the environment.

/s/
JOHN AITKEN, A.A.E.
Director of Aviation

For questions, please contact John Aitken, Director of Aviation at (408) 392-3610.