7. Fair and Reasonable Rates: Allowable Environmental Costs

Airport commenters stated that the proposed limitation of allowable costs to reasonable environmental costs should be stricken; the costs of compliance with all Federal, state, and local environmental mandates, including clean air and clean water requirements, mitigation required to obtain approvals for development projects, and all expenditures for noise mitigation should be includable in the rate base; the policy should clarify that mitigation (such as wetlands replacement) may occur on or off airports. Also, airports argued, because the airport proprietor is liable for noise damages, the sponsor's judgment in developing a noise mitigation program should be given deference. Airport commenters also argued that the limitation to *current* expenditures for environmental costs should be removed; airports should have discretion to include in the rate base reserves to fund any future liability for cleanup of environmental contamination likely to result from current operations.

The carrier view is that airport proprietors should not be permitted to prefund future environmental liability for environmental remediation, other than through documented self-insurance requirements, subject to standard industry conventions and practices.

The final policy statement adopted by the Department adds language clarifying that the following environmental costs, to the extent actually incurred by the airport proprietor, will be presumed to be reasonable costs:

- Costs of complying with Federal, state, and local environmental laws and regulations, provided that, in the case of local requirements, such requirements are applied to other similarly situated enterprises (to avoid possible impermissible use of airport revenues).
- Mitigation requirements on or off airport associated with airport development (for aeronautical use).
- Noise mitigation pursuant to an approved Part 150 program or other publicly-disclosed airport noise compatibility program;
- Costs of insurance or self-insurance for correction or cleanup of environmental damage. The Department agrees with carrier comments that considerations of forward financing of environmental cleanup costs do require some limitation on the charge to current users, and the policy limits self-insurance costs to costs incurred pursuant to a formal self-insurance program that meets applicable insurance industry standards.

8. Fair and Reasonable Rates: Facilities Currently in Use

Airports asserted that the only restriction in current law is that costs must relate to the development or improvement of an existing airport; the restriction to the costs of facilities in use is overly restrictive and not supported by law. Airports argued that land and construction costs should be recoverable before a facility is in use; the proposed policy does not even clearly permit recovery of costs for borrowing to finance improvements until project completion, which could lower bond ratings and postpone land acquisition, thereby increasing project costs.

Comair praised the currently-in-use limitation on the grounds that it would impose needed discipline on airport expansion policies that show little regard for airline profitability.

The Department continues to believe that the traditional approach of limiting recovery of costs to facilities in use is clear, easy to administer, widely accepted, and supported by judicial decisions. Accordingly, the final policy statement continues to provide that only the costs of facilities currently in use may be included in the rate base; financing costs incurred for construction, including debt service and reserves, may be recovered at the time a facility comes on line. Users may, of course, agree to incur present costs for a future facility. The policy continues to provide that current costs of planning for future facilities may be recovered as they are incurred.

9. Fair and Reasonable Rates: Asset Valuation

Airport comments: Airports commented that the proposed limitation on valuation of airport property to historic cost is unduly restrictive; is not required by existing legal interpretations; is inconsistent with existing airport practice and Department policies; is inconsistent with the objective of promoting efficient use of resources; and could interfere with the successful implementation of peak period pricing. Commenters stated that airports typically use various asset valuation methods for their assets, including current cost, fair market value, or the use of inflation indices (although few individual airport proprietors claimed to be using other than historical valuation). In addition, rates and charges for many aeronautical assets are based on percentage of gross revenue. The use of indices and gross revenue formulas is not generally expected to result in rates and charges

that reflect historical cost asset valuation.

For many assets that are fully depreciated, including terminals, the use of historic cost valuation would result in a subsidy to carriers in the form of rental rates that did not reflect the value of the facilities. In addition, a strict historic cost requirement could expose airports to claims of unjust discrimination if carriers using newer facilities are charged more than carriers using older facilities that are fully depreciated. At a minimum, some airports urge that the policy make clear that blending of asset values is permitted to avoid this problem.

Further, airports claimed that the use of historic cost valuation may distort the perception of the relative value of existing and new facilities. A new facility may fail the test of economic feasibility based on the disparity between fees based on historic costs of the original facility and those based on current costs of a new facility. Moreover, in the case of gates and other terminal facilities and other facilities such as hangars or flight kitchens, air carriers themselves recognize the value of the facilities by subleasing at rates higher than historic value. A policy requiring airports to value their facilities at historic value would allow airlines to enjoy a windfall in the form of a differential between the market rates they can obtain for subleases and rates paid to the airport based on historic cost. The public interest would be better served, airports argued, if the airport proprietor were able to capture this appreciation through market-based rates and to apply the proceeds for the development of airport infrastructure.

It was also argued that historic cost valuation could limit the effectiveness of peak period pricing. If an airport is unable to reflect the opportunity costs of its scarce assets in its rate base, the maximum peak price that can be charged may not be enough to cause traffic to shift away from the peak period.

The proposed historic cost requirement, in the airports' view, is not supported in law or FAA policy. Decisional law is clear that results, not methodology, are significant in determining reasonableness. In addition, under the *Evansville* standard, a rate is considered reasonable if based on some fair approximation of use and not excessive in comparison with the government benefit conferred. A rate based on the standard of "benefit conferred" will in most cases be different from rate based on a facility's historic cost.