PolicyAnalytics, LLC

Confidential Draft Memorandum

To: Leigh E. Morris, Chairman
William Q. Hanna, President
Northwest Indiana Regional Development Authority

From: William J. Sheldrake, President
Policy Analytics, LLC

Re: A Financial Analysis of the Gary Chicago International Airport

Date: October 9, 2012

The following analysis is provided to the RDA Board members and President in accordance with Policy Analytics' contractual relationship with the RDA and is produced at the request of the Chairman of the RDA, Leigh Morris, to address issues relevant to the financial status of the Gary Chicago International Airport, and in particular its Runway Extension Project. Within this document the designations, "GCIA", "GYY" or "airport" are understood to refer to the airport located in Gary, Indiana. The Chairman requested that the report address the following three objectives:

I. Provide a clear picture of the financing of the runway extension / rail relocation project; to its completion – The Runway Project [or the "LOI Project"]

II. Determine the adequacy of the financing for all other necessary capital investments – the Capital Improvement Plan, [CIP]

III. Develop the picture of the finances supporting the future operations of the CCIA – Ongoing Operations

The first two of these objectives have been analyzed and the results presented below. The third objective is not able to be fully addressed at this time, as the GCIA management has stated that it does not have the resources to provide detailed financial and operational data regarding future airport operations, at this time. However a brief overview of the near-term operational finances is appended to this memo.

The sources for this report are the GCIA's Sources and Uses statements for the LOI Project and the CIP, prepared in conjunction with Acacia Financial Group and Whittaker and Associates. Also, the mandated "Special District Annual Reports" [SDAR] and the airport's budget for CY 2012 and CY 2013 were provided by Airport management. In addition, the Strategic Business Plan [SBC] developed by Landrum and Brown, and the analysis of the airport's finances done by Public Finance Management [PFM] as part of the State of Indiana's "Distressed Unit Appeals Board's" processes surrounding the City of Gary's property tax appeal in 2009 were also consulted. Finally, Policy Analytics undertook an extensive analysis using its parcel level property tax model to project property tax revenues for all relevant funds.

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The Runway Project

The GCIA first discussed applying to the RDA for a grant to extend its main runway and move an inhibiting elevated rail line in 2006. The final application was presented and approved by the RDA in 2011. The project – known as the "runway project" – is deemed necessary according to the FAA for the GYY to remain a viable airport with the hope of future commercial development. The project's financial plan is shown in Exhibit A. The original request to the RDA was for $30.0 million, to help fund a projected budgeted at $153.1 million. This request was in addition to an Indiana General Assembly appropriation, made in 2006 for $20.0 million [the funds were "routed" through the RDA] for the same project.

Exhibit A

		Through 7_31_2012	2012	2013	2014	Total
Sources						
RDA - Grant & Legislative Approp	(1)	20,000,000	27,000,000	3,000,000		50,000,000
LOI (FAA funds)	(2)	20,861,016	14,138,984	5,000,000		40,000,000
Add'l Airport Revenues (TIF)	(3)	4,975,323	16,790,023	3,280,000		25,045,346
PFC Revenues from CGRAA	(4)	2,411,473	2,588,527	2,500,000	2,000,000	9,500,000
FHWA	(5)		6,000,000	-		6,000,000
AIP-Entitlement	(6)	3,150,000	1,300,000	1,000,000		5,450,000
Supplem'l FAA Proj Funding	(7)	2,852,934		-		2,852,934
State of IN	(7)	695,617	275,145	135,526		1,106,288
Airport Revenue (Interest, Lease Rev)	(7)	1,471,569	2,439	63,600		1,537,608
Debt Financing		-	-	24,715,081		24,715,081
Total Sources		56,417,932	68,095,118	39,694,207	2,000,000	166,207,257
Uses						
Agrmts/Prog Mgmt/Admin/Land		17,559,436	7,986,963	10,591,117		36,137,516
Runway, Taxiway Extension		2,747,181	14,745,561	10,144,673		27,637,415
Railroad Relocation		5,649,694	6,093,701	15,711,700		27,455,095
NS Railroad Improvements		244,634	1,755,366	20,015,000	5,000,000	27,015,000
IN Hiway Grade Sep - Enablg Proj		2,646,360	9,343,975	6,628,483		18,618,818
Powerlines Reloc - Enablg Proj		15,482,536	28,402	-		15,510,938
Railroad Relocation - CN Bridge		5,383,788	4,490,782	1,506,613		11,381,183
Tank Relocation - Enablg Proj		2,451,290	-	-		2,451,290
Total Uses		52,164,919	44,444,750	64,597,586	5,000,000	166,207,255

Notes:

(1) RDA Grant total $50m, $20m of which has already been received, $30m already approved which will be used to fund 2012/2013 projects.

(2) FAA funding grant that can be used to fund large-scal capacity projects at primary or reliever airports. The amount awarded was $47.84m of which $7.84 not shown above is to be received in 2014 and 2015 and will be used for debt repayment.

(3) Tax Increment Finance district [ADZ] administered by the GCIA.

(4) PFC Revenues are funds due from City of Chicago Dept. of Aviation [CDA] related to the Compact between the CDA and the CGRAA.

(5) Federal Highway Administration to be allocated to the GCIA for the relocation of existing rail lines to accommodate runway expansion.

(6) Airport Improvement Program Entitlement Funds based on a formula using enplaned passengers and the class of an airport per FAA. It is assumed that the airport will receive $150,000 during the forecast period, except for CY 2012 and 2013.

(7) Supplemental funds which were received and allocated in the past. It is uncertain if these funds will be available in future periods; State of IN entitlement funds, airport revenues consist of interest on deposits and revenues from lease agreements with Yellow Trucking.

(8) Total Contingency included in current budget estimate totals $6,998,191 plus $1,880,123 for savings realized in bid awards which were under current budget estimates.

Source: GCIA Finance Manager - Dated July 31, 2012; Updated per GCIA Financial Advisors October 9, 2012

<u>Exhibit A</u>

Exhibit A, above, provides an overview of the Runway Project financial plan, demonstrating the following points.

1) The project is primarily funded through grants:
   a) A Letter of Intent grant from the FAA [$47.84 million in discretionary funding].
   b) A $20 million legislative appropriation to the GCIA, which was "routed" through the RDA, and provided to the airport in CY 2007.
   c) A $30 million grant from the RDA of the RDA's "own source" revenues.

2) The next major source of funding is from revenues accruing to the GCIA's TIF district, the Airport Development Zone [ADZ].
   a) The ADZ holds accumulated balances in the amount of $25.0 million. [At the end of CY 2011 the last year of actual SDAR data available the balance in cash and investments was $21.3 million.]
   b) Bond proceeds are anticipated to fund the project in the amount of $24.7 million; the debt service for those bonds is supported by the ongoing revenues of the ADZ.

3) The Program Manager, AECOM, maintains that the current estimated total project cost, $166.2 million is the best estimate of final project cost. Again, according to AECOM there is, within that estimate, a remaining contingency of $8.9 million.

<u>**The Capital Improvement Program**</u>

The GCIA's CIP represents the planned addressing of the airports capital needs for the next five years. It includes both major and minor repair and rehabilitation items, runway and airside equipment upgrades, and large scale equipment purchases. A detailed list of the planned projects and purchases is shown in the airport's CIP Sources and Uses, provided below in Exhibit B. [The CIP dated July 31, 2012 is, per the GCIA Financial Advisors due to be updated to reflect actual project funding in CY 2012 to date.]

The CIP is funded through a combination of funding sources.

1) Revenues from the ADZ are used, however in some cases these funds may be reimbursed by Passenger Facility Charges [PFC] funding. ADZ funds are shown at an amount equal to $1.7 million.

2) PFC funds made available through the CGRAA, [the Compact] are used for capital purposes. Application must be made and reimbursement received.

3) Airport Improvement Program [AIP] funding from the FAA is subject to the level of enplanements and approval by the FAA. The Airport has not assumed the higher level of AIP funding which could be available based on achieving greater than 10,000 enplanements, after CY 2013.

4) Several "To be identified" sources of funding are also listed as part of the airport's CIP financial plan.

Exhibit B[5]

		Actual 2011	Actual/Est 2012	2013	2014	2016 [3]	2017	Total
Sources								
Airport TIF Revenues	(1)	1,115,170	624,831		-			1,740,001
FAA Discretionary w IDOT Buy-in		-		3,800,000	1,375,000	6,226,118	1,300,000	12,701,118
Other		-	300,000	-	-			300,000
PFC Applications Submitted to CDA, Pending Approval	(4)	-	840,000	3,890,000				4,730,000
To be identified			45,000	355,000	1,750,000	875,000		3,025,000
Total Sources		1,115,170	1,809,831	8,045,000	3,125,000	7,101,118	1,300,000	22,496,119
Uses								
Rehab Park'g Apron, 2011 Proj Reimb	(2)	1,115,170	354,831					1,470,001
Rehab Runway 2-20				3,800,000				3,800,000
Rehab Taxiways B & C					1,375,000			1,375,000
Rehab Taxiway A						6,226,118		6,226,118
Heavy Duty Snow Removal Truck							400,000	400,000
Snow Removal Equip Blg Expansion							900,000	900,000
Rehab Term Apron Design - Phase I	(2)		270,000					270,000
Install Parking Revenue Equipment			300,000					300,000
Runway Incursion Lights				355,000				355,000
Rehab Terminal Apron - Phase I	(2)			2,110,000				2,110,000
Rehab Terminal Apron - Phase II	(2)			1,780,000				1,780,000
Heavy Duty Snow Removal Truck	(2)		390,000					390,000
Cold Air Jet Blower	(2)		450,000					450,000
Heavy Duty Snow Broom					400,000			400,000
Cold Air Jet Blower						475,000		475,000
Heavy Duty Snow Broom						400,000		400,000
Perimeter Access Road - Phase I			45,000					45,000
Perimeter Access Road - Phase II					1,350,000			1,350,000
Total Uses		1,115,170	1,809,831	8,045,000	3,125,000	7,101,118	1,300,000	22,496,119

Notes:
1) Airport Development Zone funds used which are eligible to be reimbursed with PFC's.
2) These projects were approved by the CGRAA in 2011 and 2012; however applications have not been submitted to the airlines.
3) CY 2015 is omitted - there is no activity in that year.
4) GCIA has submitted PFC applications to the CDA which are pending submission to the FAA for approval. Internal funding from the ADZ is anticipated to be repaid when PFC's are received.
5) The GCIA Financial Advisors have stated that this CIP plan of finance will be updated to reflect 2013 and forward projects.

Source: GCIA Financial Manager - Dated July 31, 2012; updated per GCIA Financial Advisors October 9, 2012

Considerations of Financial Risk and Opportunity for the GCIA

A) The largest single source of funding for the Runway Extension Project is the GCIA's ADZ balances and ongoing revenues. Policy Analytics undertook research into the reliability of the tax base supporting the ADZ and made projections of revenue using its parcel level property tax model. The following findings are applicable:
   1) The accumulated funds [balances] that have accrued to the ADZ from prior year tax distributions are held by the GCIA and are immediately available when needed.
   2) The tax base of the ADZ was established by resolution at a time when assessed value [AV] from all classes of parcels, including residential, could be captured within the "increment" and all those classes are therefore able to contribute to the annual tax revenue distributed to the ADZ fund.

3) A review of the tax base of the ADZ – the composition of real property by class and an analysis of the largest taxpayers was undertaken by Policy Analytics. The 100 largest taxpayers represent 44.5% of the total Net Assessed Value of the district for CY 2011 and 48.6% for CY 2010. Those taxpayers have been relatively stable over the past 4 years. Only real property AV has been included within the increment.
4) For the most recent 2 years of actual data, the ADZ collected approximately 83% of the property tax revenues billed, [source is the Lake County Auditor's Form 22 for CY's 2010 and 2011].
5) Because of inconsistencies in the timing of the distribution of property tax revenues from the Lake County offices, and because of the effect of rate relief provided to the City of Gary by the State of Indiana's Distressed Unit Appeals Board, historical data from CY's 2008, 2009, 2010 and 2011 are unreliable guides to the likely amounts of property tax revenue accruing to the ADZ. Policy Analytics' estimates of net property tax revenue to the ADZ for years 2012 through 2015 were generated using its parcel level model. These estimates are exhibited in Appendix A.
6) Policy Analytics estimates that the property tax revenue net of circuit breaker credits to the ADZ in CY 2013 will be approximately 36% higher than the amounts estimated in the GCIA Sources and Uses document.
7) While the ongoing revenues to the ADZ appear both stable and growing, a bond issue supported by this source may well need credit enhancement, such as that afforded by the State's Moral Obligation, [Moral Ob]. The State of Indiana has, since 2005, demonstrated a changed policy with respect to providing its moral ob to local units of government, and economic development projects. At this time it seems unlikely that bonds issued by the CGIA's ADZ would receive this form of State credit enhancement.

B) The GCIA was asked to consider its options, should the Runway Extension Project require more financial resources and to provide some discussion of its considered contingencies. The following strategies or sources were mentioned by the GCIA.
   1) The GCIA could appeal to the FAA for an addition to the LOI discretionary grant amount. Other projects around the country certainly experience cost increases or funding shortages. The FAA is being cultivated by the GCIA for just such a request. The likelihood of a positive and significant response to this request for additional funding is not known at this time.
   2) The GCIA could attempt to increase the amount of debt issued. The current estimate is $26.7 million; however that amount could be increased based on credit availability and revenue sources.
   3) The GCIA could delay the NS railroad improvements scheduled to begin in CY 2013 and finish in 2014. Some delay in this project could substantially enhance the fiscal viability of the project's finances.
   4) The GCIA could appeal to the RDA for additional funding. Since the RDA is a major grantor to the project, and interested in its successful completion, the RDA is likely to be asked to assist if any shortfall is experienced.

GCIA Ongoing Operations

The GCIA's longer term viability as a functioning airport with some commercial potential is, first of all, dependent on the completion of the Runway Project. Without the lengthened runway, even the charter operations, like recent entry Allegiant – will find it difficult to maintain sustained operations from GCIA, and may be forced to find other airports from which to base their flights. Charter flights to Florida are possible now, because of the smaller fuel loads required. However, similar charter flights to Las Vegas – a staple of this class of carriers – is ruled out because the current short runway will not allow for the heavier fuel and passenger loads.

The following analytical points serve to summarize the issues relevant to the operational future.

1) GCIA is being positioned by the runway extension to fulfill its strategic business plan – general aviation, corporate fleets and specialty charter – with the potential for additional commercial business expansion. [Landrum & Brown, SBC].

2) The Allegiant addition promises to provide some real charter commercial activity with associated revenue, and it points to the growth path that, over the long-term provides for more substantial development.

3) Adding more carriers, like Allegiant, or substantially expanding business activities [e.g., significant cargo operations] will likely require added investment – both capital and operating. Regional airports like GCIA universally require public subsidies, usually from local, regional and state sources, in addition to FAA programmatic funding. GCIA is hampered by the loss of property tax funding – its general levy – because of the state's newly instituted rate caps, [HEA 1001-2008]. In 2007, prior to the new property tax controls, GCIA property tax revenues for both its General and Cumulative Funds totaled $1.7 million. For CY 2012 that amount is approximately $800,000, a drop of approximately 50%.

GCIA – A Fund Level Analysis

In Indiana public finance, the units of government are required to maintain their revenues and allocate their costs to specific "funds" one of which is the unit's general fund. Since a civil unit of government's ability to levy a property tax rate is tied to particular funds [and not to others] – this analysis will look at each of the property tax revenue generating funds, both the sources and the uses. This data comes from the GCIA Budgets for 2012 and 2013, the 2011 SDAR which the unit is required to submit for each CY, and estimates provided by Policy Analytics.

GCIA General Fund

GCIA General Fund		Actual CY 2011	Estimated CY 2012	Estimated CY 2013
GF Sources				
Property and In Lieu Taxes	(1)	1,011,991	693,725	677,725
Local Inter-govt		392,296	454,102	455,000
Airport Receipts		336,741	367,375	370,000
Rental of Property		848,827	895,057	900,000
Transfers and Other Receipts		106,336	165,550	170,000
Sub-total GF Sources		2,696,191	2,575,809	2,572,725
GF Uses	(2)			
Total Personal Services		976,167	1,235,026	1,285,960
Office and Other Supplies		99,956	156,059	220,045
Total Services and Charges		852,051	1,592,691	1,477,770
Other [Incl. Capital Outlay in 2012]		2,379	313,271	313,272
Sub-total GF Uses		1,930,552	3,297,047	3,297,047
GF Accumulated Balance [Includes Prior Yr Ending Balance]		1,254,852	533,613	(190,709)

Notes: (1) Property Tax and In Lieu revenues have been forecast by Policy Analytics. Other sources of revenue have been estimated assuming prior years' levels.
(2) Disbursements for CY 2011 are shown per the SDAR for 2011. For 2012 and 2013 budgeted expenditures are shown per Management's budgets for those years. The categories of expenditures are per the grouping within the SDAR. Personal Services expenditures are budget character 41xxx; Supplies are 42xxx; Other Services and Charges are 43xxx; Capital Outlays are 44xxx.

The following comments address issues regarding the GCIA General Fund:

1) GCIA does not maintain large balances in its General Fund. Capital projects are managed from the Cumulative Capital Fund or the Airport Development Zone Fund, and large balances for those projects may be accumulated there.

2) Other airport operations, those of the Fixed Base Operator, for example, are maintained in a financial sense away from the GF.

GCIA Cumulative Capital Fund

The GCIA Cumulative Capital Fund is the fund out of which the airport is managing the bulk of the Runway Project. FAA LOI and RDA grant funds are deposited in this fund and in addition, the expenditures for the CIP are made from this fund.

GCIA Cumulative Capital Fund	Actual CY 2011	Estimated CY 2012	Estimated CY 2013
Cum Fund Sources			
Property and In Lieu Taxes	158,777	103,676	101,676
Federal Inter-govt	2,750,807	21,113,104	-
State Inter-govt	83,974	286,474	85,000
Local Inter-govt [RDA]	39,292	27,000,000	3,000,000
Bond Proceeds	-	8,074,276	-
Blg, Hangar, Rental fees	66,403	63,600	65,000
Other - Incl. Interest Inc.	77,798	40,000	40,000
Sub-total Cum Fund Sources	3,177,051	56,681,130	3,291,676
Cum Fund Uses			
Personnel & Related Uses	775,149	-	
Insurance	332,889	-	
Gasoline, Parts, Repairs, Grounds	88,973	-	
Capital Outlays	5,896,289	68,581,832	6,258,993
Other	9,914	-	-
Sub-total Cum Fund Uses	7,103,214	68,581,832	6,258,993
Cum Capital Accumulated Balance [Includes Prior Yr End Balance]	12,398,124	497,422	(2,469,895)

Note: Property Tax and In Lieu revenues are forecast by Policy Analytics. CY 2012 and 2013 expenditures are shown per GCIA Management's budget documents; including a table of budgeted revenues and expenditures by fund for CY 2012 provided early in that year.

The following comments address issues regarding the GCIA Cumulative Capital Fund:

1) The Cumulative Capital Fund serves as the financing center for the airport's Runway Project. The major sources of funds for the project, FAA LOI funding, the State and RDA grants, and bond proceeds [prospective] are shown as deposited into and then expended out of this fund.

2) While the fund is depleted in CY 2013, the airport has the discretion to move other resources into that fund, in order to maintain a positive balance.

3) A table provided by GYY Management entitled "Gary/Chicago Airport, Stmt of Receipts and Disbursements, Budget Estimate 2012" shows $8.1 million in bond proceeds as Sources for CY 2012. It is unclear if this is in addition to the $24.7 million shown in Exhibit A?

GCIA Airport Development Zone [TIF] Fund

The GCIA controls a tax increment financing fund labeled the Airport Development Zone Fund. Property tax revenues derived from the district are annually distributed to the airport for its use, primarily for capital needs, including paying debt service on bonds.

Airport Development Zone Fund	Actual CY 2011	Estimated CY 2012	Estimated CY 2013	Estimated CY 2014
ADZ Fund Sources				
Property and In Lieu Taxes	7,211,356	4,408,000	4,447,000	4,509,000
Interest Income	6,900			
Sub-total ADZ Fund Sources	7,218,256	4,408,000	4,447,000	4,509,000
ADZ Fund Uses				
Debt Service		2,098,500	3,360,800	3,360,800
Capital Outlays	1,115,169	22,365,876		
Sub-total ADZ Fund Uses	1,115,169	24,464,376	3,360,800	3,360,800
ADZ Accumulated Balance [Includes Prior Yr End Balance]	21,308,617	1,252,241	2,338,441	3,486,641

Note: Property tax revenues [TIF] and debt service payments for CY's 2013 through 2015 are PALLC estimates. CY 2011 property tax revenues contained a third distribution of a partial prior year's revenues.

The following comments address issues regarding the GCIA ADZ Fund:

1) The ADZ fund revenues are the largest "own source" revenues for the GCIA. This source of funding is serves as the "gap filler" for both the Runway Project and the CIP.

2) In order for both the Runway Project and the airport ongoing capital needs to be met, the airport must be able to issue bonds based on the tax revenues projected from the ADZ. It is may be that in order for those bonds to be successfully sold the airport will need to obtain the State of Indiana's "moral obligation" or "full faith and credit" pledge for the bond issue. The State has been extremely reluctant to apply this pledge to local issues over the past 6 years.

3) Based on Policy Analytics analysis, forecast ADZ revenues could support a bond, yielding perhaps as much as $30 million in net bond proceeds, depending on rates coverage requirements and assuming the State's "full faith and credit" pledge. The airport is appears to be estimating it will need $26.7 million for the completion of the Runway Project.