

Ontario International Airport – A Recovery Plan

September 2010

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1. Introduction

The City of Ontario (“Ontario”) presents this White Paper to support its position that the success of Ontario International Airport (“ONT”) requires that local control be restored. After extensive research, it is Ontario’s belief that the most effective and expeditious means to accomplish this objective is through a mutually agreed upon modification of the existing joint powers agreement between Ontario and the City of Los Angeles.

This document also incorporates Ontario’s comments on the Jacobs Consultancy report – “Alternatives for Management and Operation of LA/Ontario International Airport” presented at the Los Angeles Board of Airport Commissioners (“BOAC”) meeting August 2, 2010. The LAWA/Jacobs report focused on ONT’s high costs, but did not get to the heart of the other problems facing ONT: An inherent conflict of interest in Los Angeles controlling LAX and ONT, overstaffing, high labor costs, a 15 percent administrative fee levied by LAWA on ONT, and a reduced budgetary commitment to airport regionalization. Nor did it set forth options that are practical or that have a reasonable probability of succeeding. This White Paper seeks to fill this vacuum while providing a framework for ONT to make a greater contribution to airport regionalization.

2. Historical Perspective

Even people in the aviation industry are often surprised to learn that ONT is operated by the City of Los Angeles' Department of Airports (also known as Los Angeles World Airports or LAWA). ONT is located 35 miles east of downtown Los Angeles in a different city and county from Los Angeles. An understanding of how this airport came to be controlled by Los Angeles is necessary to appreciate its current status as a secondary airport in the LA Basin and to understand its potential as an integral part of the Southern California regional airports system.

The airport traces its origin to 1923, making it one of the oldest in the nation and the state. This was five years before Mines Field began operations at the current location of LAX. Dirt runways were replaced with two concrete runways in 1942 to support the nation's war effort. By the mid-1950s, Lockheed, Douglas and Northrop had major aircraft facilities at ONT. During this era, commercial air service in Southern California was limited to Burbank Airport until 1946 and thereafter at Los Angeles Municipal Airport, later to be renamed Los Angeles International Airport.

With the dawning of the jet age in 1959, commercial air service became vastly more popular. Airlines began to expand their fleets. While LAX remained the principal airport serving Southern California, there were often times when it was shrouded in fog, requiring flights to divert to ONT. As many as 60 days a year, passengers and luggage were bussed between ONT and LAX.

Because much of the annual activity at ONT during the 1960s was accommodating diverted airplanes, the cities of Ontario and Los Angeles felt it would be in the best interests of the Southern California region if Los Angeles took responsibility for operating the airport. In addition, Los Angeles was expected to bring more air service to ONT, thereby attracting businesses and creating jobs. Discussions to this end began in the early-1960s, resulting in a "Contract between the City of Los Angeles and the City of Ontario for the Joint Exercise of Powers in Relation to Ontario International Airport" ("JPA"). As memorialized in the Agreement of 1967, the parties felt that "considerable benefit would result to ONT and LAX, to the two cities and to the users of air transportation into and out of Southern California" from the arrangement.

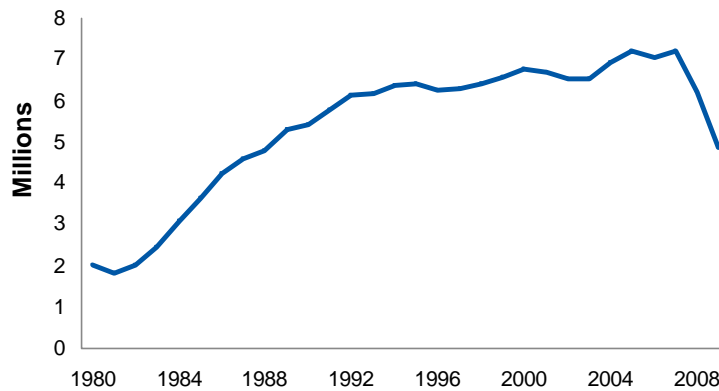
Section 9 of the JPA stated: "Los Angeles shall exercise its best efforts to attract and obtain additional regular scheduled airline service for ONT and shall immediately, under approval of this Agreement, apply to the Civil Aeronautics Board for change in the certificates of the scheduled carriers presently serving Los Angeles to specify ONT as a joint-use airport or hyphenated point with LAX."

From the signing of the JPA in 1967 until deregulation of the airline industry in 1978, the two airports were treated the same by the Civil Aeronautics Board for the purposes of airline route authorities and the setting of airfares. Thus, an airline authorized to serve LAX could also serve ONT under the same route authority and with the same air fares. Air service soon began to take off and by 1971 the airport was serving more than 1 million passengers a year.

The Los Angeles Department of Airports operated its three airports (LAX, ONT and Van Nuys Airport) as a single financial entity. This meant that all revenues from the three airports were deposited in a single airport account and all expenses were paid from that account. ONT generated sufficient revenues to cover its expenses and also to repay Los Angeles for its investments in ONT which from 1967 to 1985 totalled approximately \$4 million.

As shown on this chart, ONT passenger traffic continued to grow through the 80s and 90s as airline deregulation produced greater competition and lower fares. About a dozen LAX airlines also operated passenger flights at ONT to serve the rapidly growing Inland Empire.

ONT Passengers
1980-2009



By 1985, the airlines and LAWA determined additional facilities were needed to keep pace with the passenger growth rate. A Supplemental Agreement to the 1967 JPA was negotiated for the “Acquisition of Ontario International Airport by the City of Los Angeles.” That Agreement acknowledged the prior \$4 million payment by Los Angeles (which was subsequently fully repaid by ONT) and cleared the way for LAWA to begin development of a Master Plan to meet the airport’s long-term needs and provided future air service capacity for Southern California.

Section 14 of this Agreement stated “that both Los Angeles and Ontario recognize the continuing necessity for and hereby agree to cooperate with each other in carrying out the purposes and objectives of the Joint Powers Agreement which it is agreed shall remain in full force and effect.”

As the planning continued into the early 1990s, a major dispute arose at LAX between the airlines and LAWA relating to LAWA’s use of airport revenues and its desire to impose a “commercial compensatory” methodology for setting airline rates and charges at LAX. ONT was not involved in that dispute. Instead, it remained a stand-alone “residual” airport where the airlines’ rates and charges were adjusted periodically to ensure the airport broke even and did not require any subsidy from LAWA. This occurred beginning in 1994.

Airline rates and charges at ONT were extremely low through the 1990s, thanks to low overhead and lack of significant debt service payments. This was typical of secondary airports in the United States and the reason JetBlue Airways chose ONT as its first West Coast city in 2000. A second JetBlue flight was added in 2001 and plans announced for a third flight as part of a gradual buildup of its West Coast schedules.

As planning for the new ONT facilities turned to how to pay for them, the airlines and LAWA agreed to a plan using Passenger Facility Charges that would help keep operating costs as low as possible after the new facilities opened.

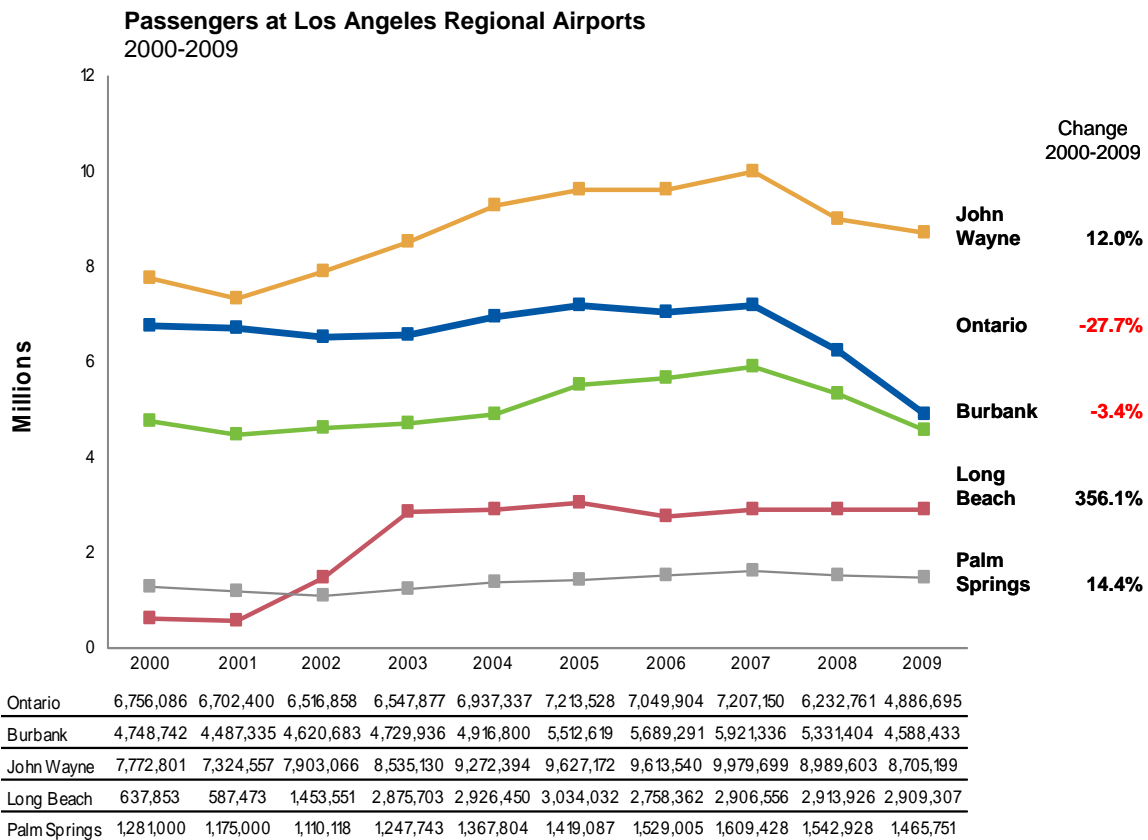
In the early 1990s, federal legislation created the ability for airports to charge a Passenger Facility Charge to be collected by the airlines in the ticketing process with funds held in trust by the airport sponsor for approved capital projects. At \$3 per enplaned passenger, LAX collected several hundred million dollars in PFCs over the course of several years. With only a limited number of LAX capital projects eligible for use of the PFC funds, the airlines serving ONT (that also served LAX) suggested using \$125 million of collected PFCs at LAX as a down payment on the new ONT facilities. Because the same airlines accounted for the vast majority of PFC collections at both ONT and LAX, it made sense to use some LAX PFC funds for the ONT terminal project. The international airlines at LAX who did not serve ONT also agreed to the plan after additional PFCs were allocated to LAX projects benefiting them. The FAA approved the specific use of PFCs and funds were transferred to the ONT terminal project. This permitted the project to go ahead with limited need for debt financing; as a result, ONT today enjoys one of the lowest debt service ratios among medium hub airports.

Nevertheless, while debt service costs were kept low, LAWA made a number of decisions that dramatically increased costs, including staffing the new facilities with City of Los Angeles employees, bringing in-house functions such as janitorial and grounds keeping that are frequently contracted out, and imposing a burdensome administrative charge. These decisions would rapidly lead to high personnel costs that would make it much more expensive for airlines to serve ONT.

3. Market Analysis

ONT is located in one of the fastest growing regions of the U.S., serving a population of nearly 5 million people in San Bernardino and Riverside Counties and portions of north Orange County and east Los Angeles County. For the broader region, ONT is generally considered the most promising solution for Southern California’s future airport capacity needs because of its ability to accommodate a large increase in air service in a region where other airports have very limited capacity to grow.

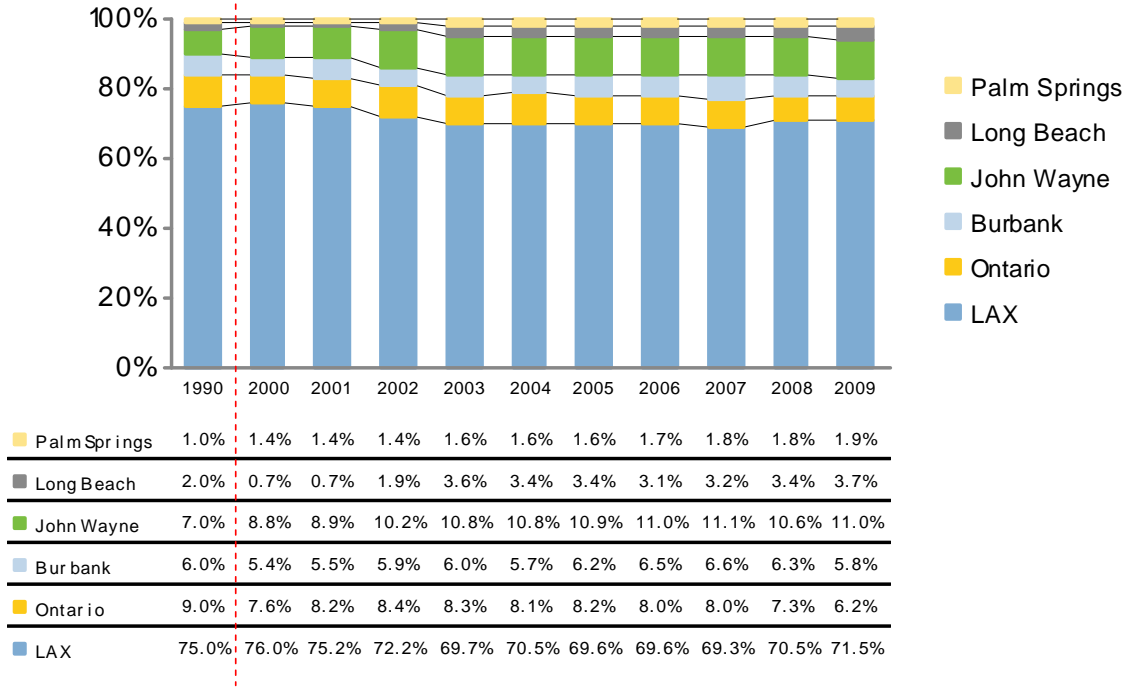
After experiencing significant growth during the ‘80s and ‘90s, ONT entered 2000 on solid footing. As illustrated below, however, by 2009, ONT had nearly 28% fewer passengers than in 2000 – a dismal record in comparison with the other Los Angeles area airports.¹ The number of ONT passengers – which approached that of John Wayne in 2000 and 2001 – now amounts to only slightly more than half of John Wayne’s. Burbank, which handled far fewer passengers than ONT in 2000, is now about the same size as ONT.



¹ Los Angeles area airports include LAX, Burbank, John Wayne, Long Beach, and Palm Springs. San Diego is not included as it serves a separate metropolitan area.

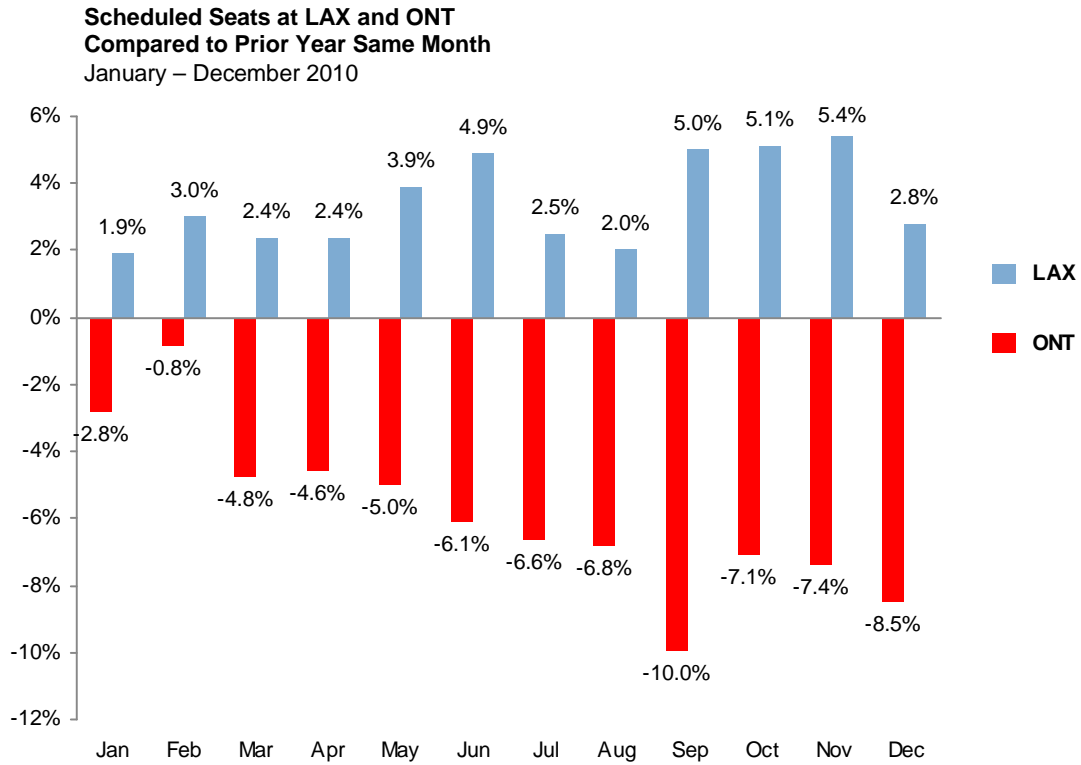
As ONT passengers have declined in absolute numbers, so has ONT’s share of the Los Angeles region’s air market. Despite LAWA’s stated policy and commitment to promote regionalization – the greater use of regional airports other than LAX – LAX’s share of passengers in the Los Angeles region has actually increased over the past seven years from 69.7% to 71.5%.

Passenger Share of Southern California Airports
 LAX, Ontario, Burbank, John Wayne, Long Beach, Palm Springs



Source: Los Angeles area airports

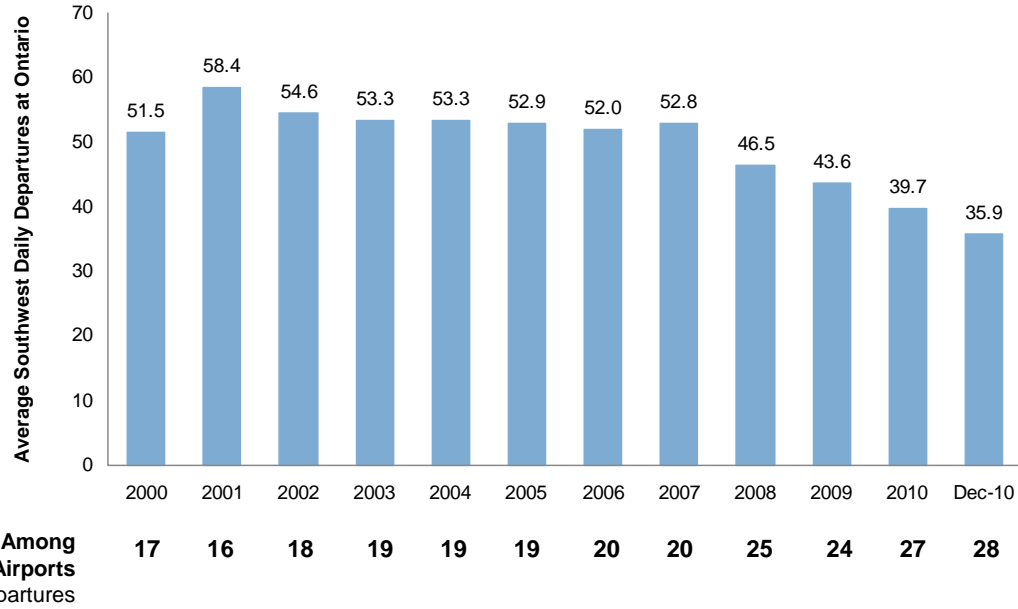
Published airline flight schedules for ONT for 2010 show that ONT continues to lose air service and will experience even deeper cuts during the 2nd half of the year. As ONT offers fewer flight options, it becomes less attractive to travelers who choose instead to fly from LAX and other area airports. This downward cycle becomes self-reinforcing and makes ONT increasingly vulnerable to further cuts. Meanwhile, as ONT continues to decline, LAX air service has grown each month in 2010 and will continue to do so for the remainder of the year.



Source: Official Airline Guide as of July 30, 2010

ONT’s largest airline, Southwest – which also serves LAX, Burbank, and John Wayne airports in the Los Angeles area – continues to cut service at ONT. As a result, ONT, which ranked as the 17th largest airport in Southwest’s system in 2000, will have slipped 11 places to 28th as of this December.

Average Southwest Daily Departures at ONT
 Each July & as Scheduled for December 2010



Source: Official Airline Guide as of July 30, 2010

Other changes since 2000:

- In 2000, ONT attracted its first non-stop service to Canada (Toronto) and Mexico (Mexico City and Guadalajara). Over the next three years, it attracted additional service to Hermosillo and Mexico City, as well as cargo service to China. As of February 2010, however, ONT has lost all international service, along with the Customs and Border Patrol staffing that is very difficult to obtain and that would be needed to accommodate international service in the future.
- JetBlue, which originally initiated its service to Southern California at ONT in 2000, now serves three Los Angeles area airports – LAX, Long Beach, and Burbank – but not ONT.
- Of the 100 largest U.S. airports, ONT’s performance in terms of passenger growth since 2007 ranked 98th.

- As a secondary airport in a large metro area, ONT’s airlines would normally include multiple low cost carriers. Instead, all the major low cost carriers in the Los Angeles area now serve LAX, while Southwest is the only low cost carrier remaining at ONT (see chart below).

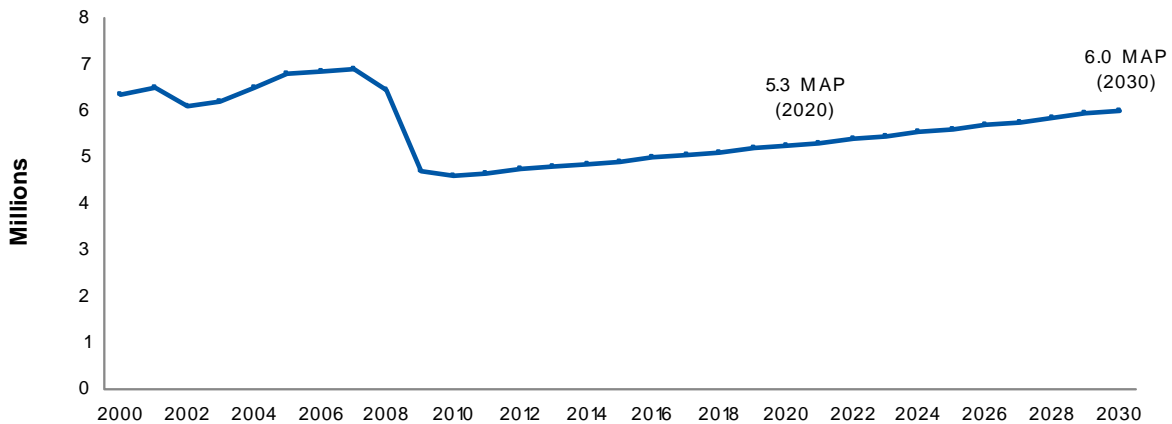
Low Cost Carrier Passengers at LAX and ONT
 2009 Domestic O&D

	LAX	ONT
Southwest	6,151,260	2,560,150
Virgin America	1,601,610	
AirTran Airways	504,340	
Frontier Airlines	437,980	
Allegiant	218,950	
JetBlue	168,740	
Spirit Airlines	127,040	
Midwest Express	76,440	
Sun Country Airlines	53,680	
	9,340,040	2,560,150

Source: Domestic O&D Survey 2009

Based on recent performance and trends, the FAA projects that ONT passengers will reach only 6 million by 2030, a figure that ONT passed in the ‘90s and that is 17 percent lower than ONT’s passenger volume was in 2005. Regardless of the accuracy of that forecast, there is reason for grave concern about ONT’s future.

ONT – FAA Passenger Forecast
 2009-2030



Source: FAA TAF 2009-2030; Passengers = Enplanements x 2. FAA actual 2000-2008; FAA forecast 2009-2030

What is causing ONT’s air service decline? Can an effective recovery strategy be developed and implemented?

4. The Problem

In major metropolitan areas with multiple airports, the economics of the airline business favour large scale operations at the primary airport – in this case LAX. Successful secondary airports in metropolitan areas with multiple airports almost invariably share two characteristics:

1. Substantially lower costs than the primary airport. Especially during the current downturn when primary airports are less congested, it is more important than ever that secondary airports maintain their cost advantage; and
2. Aggressive marketing campaigns for air service that recognize the secondary airport must compete with the primary airport and other airports in the region for passengers and flights.

As discussed below, LAWA's management of ONT has burdened the airport with the highest costs in the region and among the highest in the country.

At the same time, LAWA has made drastic cuts in ONT's marketing efforts, slashing the resources devoted to ONT market by 85% since 2007.

Whether these facts reflect a deliberate LAWA policy to develop LAX at the expense of ONT is unknown. Whether deliberate or not, the result is the same – ONT has extremely high and uncompetitive costs, and has sharply curtailed its marketing efforts.

A. ONT's Extremely High Airport Costs

From an airline perspective, airport costs are typically measured in terms of the Cost per Enplaned Passenger (CPE). The CPE is the sum of the charges paid by the airlines to the particular airport divided by the number of passengers departing from that airport. The most recent reported U.S. median CPE was \$6.76 for FY08². In budget information provided by LAWA to the City of Ontario, ONT's CPE is projected to be approximately \$14.50 in the current fiscal year, or more than double the U.S. median. The LAWA/Jacobs Report provides an even higher ONT CPE estimate of \$16 for 2010.³

The airlines are not able to charge higher fares at ONT to make up for the higher ONT airport cost. (In a region with competing airports, travelers are not willing to pay higher airfares to fly from ONT than other area airports.) Thus ONT's higher cost reduces the airlines' ability to make a profit at ONT. And the nearly \$8 *difference* between ONT's CPE and the U.S. median exceeds the airlines' total average profit per enplaned passenger.

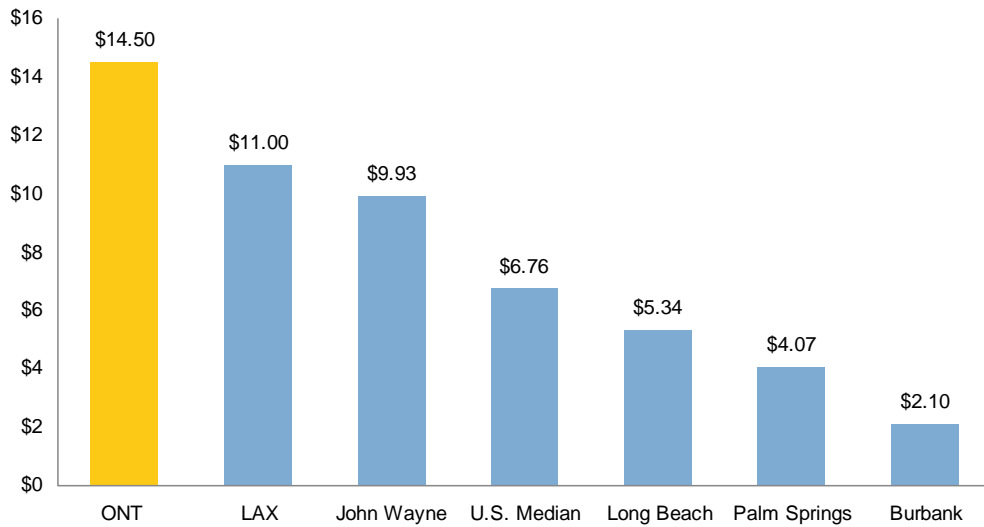
² U.S. Airport Medians for FY 2008, Moody's U.S. Public Finance, November 2009.

³ See *Alternatives for Management and Operation LA/Ontario International Airport*, August 2, 2010, p.9.

As widely reported, ONT's projected CPE for the current fiscal year exceeds that of all airports in the region. The LAWA/Jacobs Report⁴ shows that ONT's CPE is the highest among the 31 medium-size airports it evaluated. A broader analysis shows that ONT's CPE is the 2nd highest among the 69 airports served by Southwest Airlines.

Recent cost estimates for ONT, LAX, and the other Southern California airports are provided below.

Cost per Enplaned Passenger
Most Recent Fiscal Year



Source: Airport financials, press reports, FAA Form 127

CPEs are somewhat of a moving target as airline enplanements change and airports embark on major capital programs. As discussed below, although ONT's CPE also will rise and fall as enplanements change, the airport is fortunate to have a low level of debt, and therefore should have a greater ability than most airports to reduce costs during periods of declining enplanements.

B. The Role of Low Costs in Attracting Additional Air Service

Examples of successful secondary airports in large metro areas include: BWI, where lower costs were a strong factor in attracting Southwest's major operation there over Washington Dulles; and Ft. Lauderdale, where lower costs led to the development of LCC service there while Miami has none. Chicago Midway Airport, Houston Hobby, Boston Manchester, and Dallas Love Field have all achieved success by having much lower costs than the primary airports in these metropolitan areas.

⁴ See *Alternatives for Management and Operation LA/Ontario International Airport*, Jacobs Consulting, August 2, 2010, p. 9.

Low cost carriers, such as Southwest, JetBlue, AirTran, Allegiant, Spirit, and Frontier, which offer a simplified fare structure and lower average fares, are the most likely candidates for growth at ONT. These carriers are also the most likely to consider airport costs as an important factor in their air service decisions. ONT's current high costs present a significant hurdle to the expansion of air service.

As an example, Allegiant – perhaps the most cost-sensitive of all carriers – made the unexpected decision to serve LAX instead of ONT based at least in part on LAX's lower costs. Allegiant's decision to serve LAX beginning in May 2009 stands in contrast to its actions in other large urban areas, such as Phoenix, where it serves a secondary airport, Williams Gateway; and Tampa, where it serves a secondary airport, St. Petersburg. Allegiant has recently expanded service in the LA region by initiating service to four cities from Long Beach, another lower cost airport.

Although there is no guarantee that lowering ONT costs will result in more air service, having low costs gives ONT a fighting chance to reverse the recent loss of air service and to begin a long-term growth trend. With lower costs more typical of a secondary airport in a large metropolitan area, ONT would be well-equipped to make its case for additional or new service to Southwest, JetBlue, Allegiant, and other low cost carriers.

The LAWA/Jacobs Report acknowledges the importance of lowering ONT's costs:

“Reducing CPE alone would not result in an increase in air service from incumbent airlines in the short-term, but doing so could be an important step in the long-term growth in air service from incumbent airlines and in attracting competitive air service from new-entrant airlines.”⁵

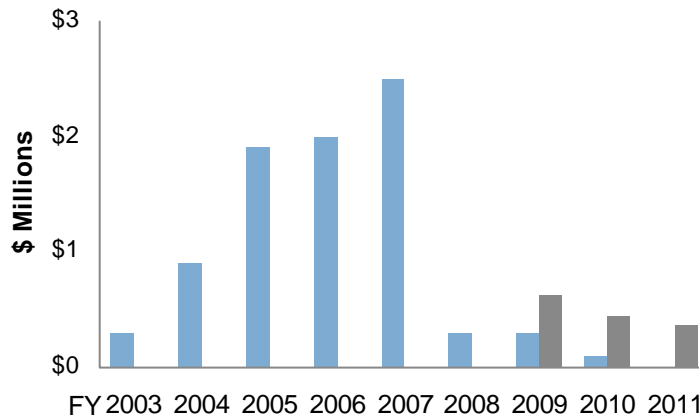
C. LAWA's Drastic Reduction of Air Service Marketing at ONT

Apart from having low costs, nearly all successful secondary airports have engaged in aggressive air service marketing campaigns. LAWA did so as well for ONT until 2007, when it changed course and slashed the resources devoted to ONT marketing efforts.

Precise figures on ONT marketing expenses are not broken out in LAWA's budget, but the information below is believed to be reasonably accurate.

⁵ See *Alternatives for Management and Operation LA/Ontario International Airport*, Jacobs Consulting, August 2, 2010, p. 3.

Estimated ONT Air Service Marketing Expenditures



Source: Estimated based on industry sources and LAWA budget analysis; 2009-2011 figures in grey provided by LAWA.

Figures for FY2003 through 2008 are based on historical information and industry sources, with estimates going forward. Separate figures in grey for FY2009-2011 are as provided by LAWA

After spending in the range of \$2-3 million per year for ONT air service marketing during FY 2005-2007, LAWA slashed that figure to less than \$400,000 for the current fiscal year, a reduction of approximately 85%.

LAWA has never explained this deliberate decision to curtail air service marketing at ONT. It is, however, inconsistent with LAWA pledges to support regionalization and has been harmful to air service development at ONT. During this same period, many U.S. airports were increasing the resources devoted to air service marketing in the face of growing competition among airports for new air service.

Other LAWA actions further illustrate its lessening commitment to ONT. For example, for many years, the LAWA Board of Airport Commissioners routinely held two Commission meetings each year in Ontario to demonstrate its commitment to ONT and regionalization. The BOAC has not held a meeting in Ontario since October 2007 (almost 3 years).⁶

D. Understanding the Components of ONT's Costs

The charges paid by the airlines serving ONT are determined by totalling the airport's operating expenses and debt payments, and subtracting any revenue the airport receives from sources such as airport parking, rental car fees, and airport food and retail. The balance is what the airlines must pay.

⁶ LAWA reports that it discontinued ONT meetings based on a City Attorney opinion that prohibits LAWA from acting on any LAX or Van Nuys items during meetings held outside of Los Angeles.

To determine why ONT's costs are so high, it is necessary to briefly review the airport's operating expenses, debt payments, and non-airline revenue. Although the LAWA/Jacobs Report suggests that additional study is needed to determine why ONT's costs are so high, even a cursory analysis of the airport provides a clear answer. We begin with a review of ONT's debt.

E. Airport Debt – Not the Problem

Some airports have high costs as a result of the substantial debt incurred as part of large capital development programs. The debt incurred in building the Denver Airport in the early 1990s made it a particularly costly airport for many years, as did the debt required to finance San Francisco's international terminal in 2000. Debt service requirements sometimes make up more than half of total operating costs at airports with major capital programs.

ONT is fortunate in that it has little debt. Fitch Ratings, in its March 2009 review of ONT, highlights the airport's "low debt levels" and "very modest and level debt profile (with debt service payments representing only 8% of total operating revenues in fiscal 2008)." Fitch notes as well that the "airport has no major capital projects over the next 5-10 years and intends to fund maintenance capital projects from airport cash and from passenger facility charge revenues and grants."

The median level of airport debt for U.S. airports was \$78 per O&D passenger in fiscal 2008, according to Moody's⁷. For Ontario, the comparable figure was only \$23 in airport debt per enplaned passenger. For the current fiscal year, the ONT figure will have risen to about \$34 because of the declining number of passengers. Even so, ONT's outstanding debt is only 44% the level of the median U.S. airport. In short, despite ONT's passenger declines, debt is not the cause of its high costs. Other things being equal, ONT's low debt means it should have lower than average costs.

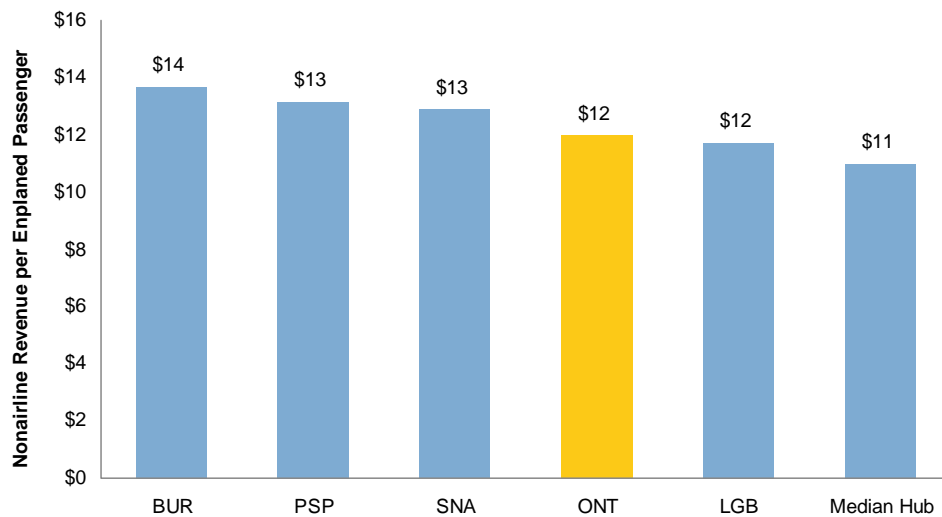
F. Revenue from Non-Airline Sources – Not the Problem

The more revenue collected from sources such as airport parking, rental car fees, airport food and retail, and other "non-airline" sources, the lower the fees the airlines must pay.

Although there is certainly room for improvement in some aspects of ONT's non-airline revenue management efforts, it turns out that ONT's non-airline revenue per enplaned passenger is slightly higher than the medium-hub airport average of \$11. This is primarily because ONT's parking revenue and rental car rental are higher than average. These sources of revenue more than compensate for ONT's lower than average food & beverage and retail revenue.

⁷ *U.S. Airport Medians for FY 2008*, Moody's U.S. Public Finance, November 2009.

Nonairline Revenue per Enplaned Passenger FY 2008



In summary, a lack of non-airline revenue is not the cause of ONT's high costs. Other things being equal, ONT's higher than average non-airline revenue means that it should have lower than average airline costs.

G. Sky High Airport Operating Expenses

If ONT has low airport debt and above average non-airline revenue, what is the reason for ONT's high costs? The short answer is that ONT has extremely high operating expenses as a result of:

- A much larger workforce than comparable airports
- The burdensome LAWA administrative charge
- Much higher compensation levels than at comparable airports

For U.S. airports, the median level of operating expenses per enplaned passenger for FY 2008 was less than \$14⁸. For ONT, operating expenses per enplaned passenger have ranged from \$29 to \$33 over the past several years – and even after cost and staff reductions at ONT will be in the \$29 range. Thus, as the LAWA/Jacobs Report accurately states, even after cost cutting –

"ONTs total operating expenses per enplaned passenger are more than twice the average for U.S. medium hub airports"⁹.

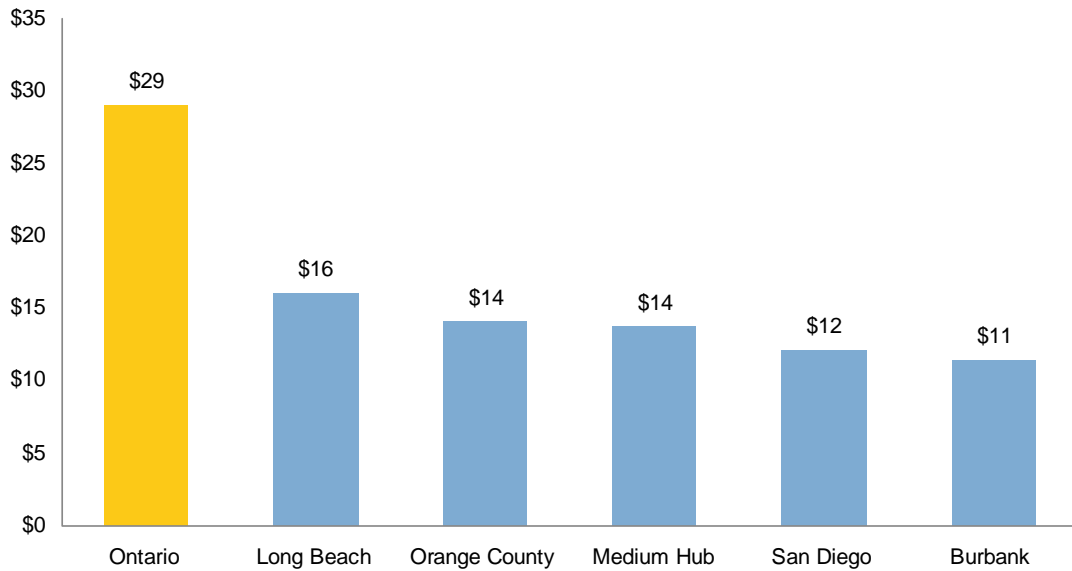
⁸ *U.S. Airport Medians for FY 2008*, Moody's U.S. Public Finance, November 2009.

⁹ See *Alternatives for Management and Operation LA/Ontario International Airport*, August 2, 2010, p.11.

The LAWA/Jacobs Report shows that in comparison to ONT’s \$29 operating expense, comparable airports had operating expenses ranging from \$9 to \$17 per enplaned passenger, with all but one of the comparable airports below the \$15 level.¹⁰

The chart below shows the operating expense per enplaned passenger at Los Angeles area airports and San Diego.

Operating Expense per Enplaned Passenger
Most Recent Fiscal Year



Source: Airport financials, Fitch ratings reports, FAA Form 127

Stated differently, assuming that ONT had achieved the medium-hub airport cost average at its existing enplaned passenger level, ONT could generate over \$31 million in cost savings, or a cost reduction in the range of \$13 per enplaned passenger.

¹⁰ See *Alternatives for Management and Operation LA/Ontario International Airport*, August 2, 2010, p.11.

H. Too Many Employees, at High Average Compensation Levels, and Additional Millions (\$) for Administrative Services

Comparing the number of employees at different airports has certain limitations because the degree of outsourcing differs.¹¹ Nevertheless, most airports operate within certain ranges, and in terms of employee staffing, ONT is in a class by itself.

ONT has budgeted for 302 employees for the fiscal year beginning July 2010, an extremely high number that is discussed below. In addition to budgeting for those employees and other operating expenses, ONT pays LAX an administrative fee of 15% of its operating expenses. For the fiscal year that began July 2010, the administrative fee will be \$8.7 million. We do not know what services are provided in exchange for this charge. Although there are certainly some important functions that LAWA provides ONT, such as legal, risk management, etc., the magnitude of the administrative charge raises questions as to the value provided – and particularly so when viewed in conjunction with ONT’s already high budget for wages and benefits.

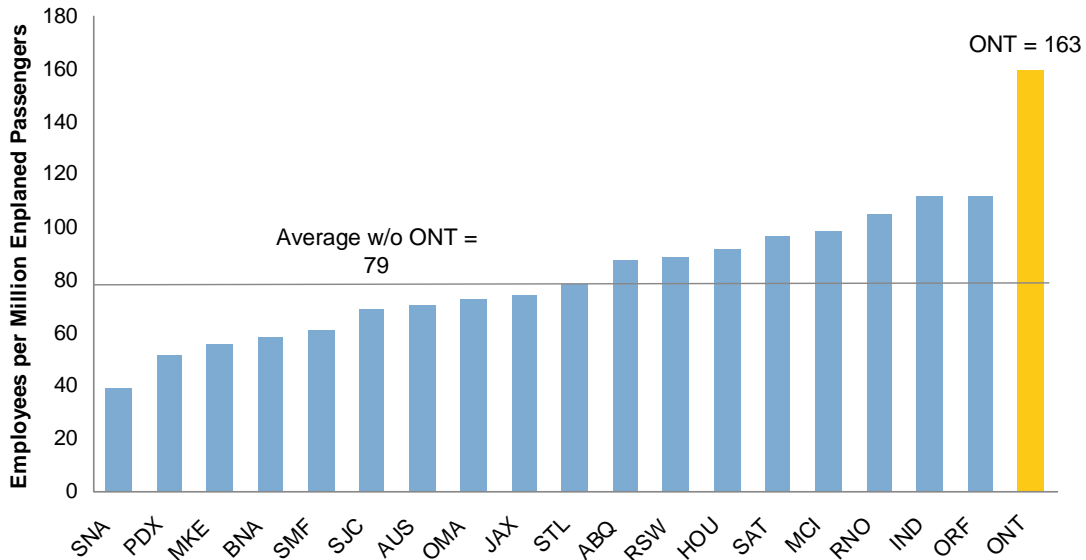
ONT’s compensation budget for the current fiscal year is \$30.9 million, which amounts to \$102,400 per employee. Taking into account the administrative fee, ONT’s true employee count is really the 302 employees budgeted plus 85 additional LAWA employees that it pays for with the \$8.7 million administrative fee (85 x \$102,400 is \$8.7 million).¹² The true total ONT employee count of 387 is more than double John Wayne’s staff of 175, more than three times Long Beach’s staff of 124, and more than San Diego’s staff of 355 (SAN has three and a half times as many passengers as ONT).

Shown below for 18 medium-size airports is the number of airport employees per million enplanements, which range from 52 to 112 – with an average of 79 employees per million enplaned passengers. The ONT estimate of 163 employees per million enplaned passengers is more than double the average of the other airports.

¹¹ At Burbank, for example, most airport functions have been outsourced, and total airport salaries and benefits are only \$2.4 million compared with contractual services that are seven times that amount.

¹² Both the employee count and the administrative charge are down substantially from the year before when LAWA budgeted for 366 employees and a \$10.2 million ONT administrative charge.

Employees per Million Enplaned Passengers – Medium U.S. Hubs
 Most Recent Fiscal Year



Source: Analysis of reported airport staffing

Note as well that among medium size airports there is little correlation between the size of an airport and the number of employees reported per million enplanements. In other words, smaller airports do not necessarily have more employees per million enplanements.

Using the ratio of 79 employees per million enplanements and applying that ratio to ONT’s projected 2.37 million enplanements shows that ONT should have approximately 187 employees – assuming that the administrative charge goes away – and not 302 as currently budgeted. If ONT continues to pay an \$8.7 million administrative charge, then ONT would need to reduce its staff from the current level of 302 employees to only 102 employees to reach an average staffing level. (The administrative charge alone adds \$3.68 per enplanement to ONT’s costs – which is more than Orange County, San Diego, or Burbank paid in total compensation and benefits per enplanement in FY2008.)

Apart from the sheer number of employees, the ONT budgeted average employee compensation of \$102,400 is the highest of any airport in the region, with other airports having total average compensation at least 15% lower. And this figure may understate true average ONT compensation because many of ONT’s core senior management functions are provided by LAWA. Even the airport manager position at ONT is split half time with Van Nuys Airport – an unusual arrangement for a medium hub airport.

LAWA's management has made substantial cuts in ONT's operating costs.¹³ To have made such efforts only to achieve little progress in improving ONT's costs suggests that the LAWA organizational structure is simply not suited to operating an airport such as ONT which must have a competitive cost structure to have a realistic chance of succeeding. The LAWA/Jacobs Report suggests as much in its consideration of outsourcing the majority of ONT operations.

¹³ LAWA notes that there were 450 LAWA employees at ONT in 2007, and therefore the 2011 budgeted number of 302 represents a decrease of nearly one-third.

5. Transfer Options

This section discusses the three options set out in the LAWA/Jacobs Report, as well as the most logical option of transferring management control of the airport back to the City of Ontario.

Each option is evaluated using the following criteria:

- (1) Will the option result in ONT achieving a competitive cost structure?
- (2) Will the option result in ONT's management aggressively marketing the airport?
- (3) Does the option assure that management will devote the time and attention needed to develop ONT to its full potential?
- (4) Does the option assure that ONT's interests will be paramount and not subject to conflicting priorities?

A. LAWA/Jacobs Report Options

The following three options are discussed in the LAWA/Jacobs Report:

LAWA continues to manage and operate ONT – LAWA would continue to seek ways to lower airline costs and increase non-airline revenues.

This option is a continuation of the status quo that has not worked to date and fails to meet any of the four criteria outlined above—cost reduction, aggressive marketing, management focus, and conflict avoidance.

3rd Party Terminal and Parking Concession Agreement – LAWA would outsource the operation and maintenance of the terminal facilities, concession program, public parking, and rental car.

This option partially addresses the first criterion and none of the others. By outsourcing portions of the airport to a more efficient operator, it would lower airport costs. However, it does not outsource the entire airport, including portions that consume significant operating resources, and therefore may not achieve the cost reductions required. In addition, it does not address the other criteria listed above.

Long Term Concession Agreement – LAWA would lease the airport for 40-60 years. Although the LAWA/Jacobs Report does not mention the FAA's privatization program, the description suggests that vehicle would be used.

This option may or may not ultimately lead to a competitive cost structure for the airlines at ONT. So far, there have been no successful privatization efforts in the U.S. so this is unproven territory. What we do know, however, is that even if successful, the privatization process will take at least 2-3 years. ONT cannot wait that long to make substantial progress in reducing costs and to begin to aggressively promote the airport. Each month that passes means less air service at

ONT and a more difficult recovery. Depending on the structure of the deal, this option may satisfy the other criteria listed, at least if Ontario is the public agency sponsoring the privatization."

B. Transfer of Control to Ontario

The City of Ontario once used the JPA to transfer control of ONT to the City of Los Angeles. The same JPA may be used to transfer management and operational control of ONT back to the City of Ontario. Ontario is committed to taking whatever steps are necessary to assure that this vital economic engine is reinvigorated through the creation of a low-cost airport that aggressively markets the airport and region. For Ontario, there is no doubt as to the airport's highest priority of attracting new service, nor will there be the appearance of a conflict of interest.

6. The Ontario Imperative

It is a hopeful sign that Los Angeles recognizes the need for a different approach to the management and operations of ONT. Ontario strongly believes that the management and operating responsibility for ONT should be transferred to the City of Ontario through a modification of the JPA as described in this White Paper. This option provides the greatest opportunity to ensure the long-term viability of ONT while achieving the mutual goal of airport regionalization.

There must be a sense of urgency as the two cities work together cooperatively to find a way to reverse the downward decline of air service and passenger traffic at ONT. Since 2007 passenger traffic at ONT has plummeted more than 32 percent. Adding to the need for immediate action, airlines serving ONT have announced flight schedule reductions of nearly 8 percent in the second half of 2010. In economic terms, the decline in air service at ONT from 2007-2009 has meant the loss of over \$400 million to the Inland Empire regional economy and the loss of over 8,000 jobs.¹⁴

In 2006, LAWA affirmed its commitment to regionalization as part of the settlement of a lawsuit challenging the Master Plan for expansion of LAX. There, LAWA expressly agreed to “develop a regional strategic planning initiative to encourage the growth of passenger and cargo aviation activity at under-utilized, LAWA owned, commercial airports in the region (currently Ontario International Airport and Palmdale).”

It is admirable that LAWA has begun to reduce operating costs at ONT. It is crucial that the City of Ontario continue this process as it aggressively markets the airport. There also must be recognition that there is the appearance of a conflict as a result of LAWA owning and operating competing airports in the current and future Southern California economy. This conflict must be addressed as a prerequisite to achieving true airport regionalization and restoring ONT as an economic engine for the region.

Since 2001, LAX has declined from the 3rd busiest airport in the world to the 7th. In 2009, it served 56.5 million passengers, a loss of 5.9 million passengers since 2007 and 10.8 million since 2000. Ontario understands LAWA’s need to focus attention and resources on rebuilding LAX traffic even as it mounts the largest capital improvement program in the airport’s 83-year history.

Returning ONT to local control will also promote airport regionalization, a key initiative of Los Angeles Mayor Antonio Villaraigosa. Regional airports in Southern California under local control have rebounded from 9/11 and weathered the recessionary economy. Regional airports

¹⁴ Estimated total economic impact of ONT passenger air service; 2007: \$1.27 billion; 2009: \$860 million; loss of \$410 million. Estimated total jobs created by ONT: 2007: 25,081; 2009: 17,006; loss of 8,075 jobs. Source: Oliver Wyman analysis.

under absentee control – ONT and Palmdale Regional Airport – have not. Adding to the importance and urgency of airport regionalization is SB 375. Without a healthy ONT, the region will be challenged to develop a successful sustainable community strategy under SB 375 which the California Air Resource Board would approve.

Under local control, ONT will simultaneously reduce its cost structure and increase its marketing, advertising and promotion spending to provide the airport capacity Southern California needs in the long term to protect its tourism economy. Other airports in the region are constrained. John Wayne Airport has a passenger cap. Long Beach Airport has a noise cap. Bob Hope Airport is constrained by its facilities and staunch opposition to airport expansion from the City of Burbank. Palm Springs Airport's ability to assume a greater market share is limited by its distance from the regions' major population centers. ONT is the only airport in Southern California that is unconstrained, and where there is political and community support for greatly expanded operations.