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American Airlines®

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December 29, 2000

Passenger Facility Charge Branch (APP-530)
Attn: Joseph Hebert
Airports Financial Assistance Division, Room 619
800 Independence Avenue, S.W.,
Washington, DC 20591

FAA-02-13918-6

Dear Mr. Hebert:

Attached please find American Airlines voluntary submission of cost data and cost definition information (Attachment I) pertaining to the costs incurred by American Airlines in collecting, handling, and remitting Passenger Facility Charge (PFC) Revenue. Please note that the associated costs are those of American Airlines and American Eagle that are directly associated with PFC collection, handling, remitting, reporting, record keeping, and auditing.

Also, please find attached An Agreed Upon Procedures Report issued by Ernst & Young, LLP. This report represents an Independent Review of American Airlines and American Eagles 1999 costs associated with the collection, handling, and remitting, reporting, record keeping, and auditing of PFC's.

This information is being provided to the FAA and the OIG under House Report 106-513, which accompanies AIR-21, Section 105

“Under the law governing passenger facility charges, FAA is directed to prescribe regulations which establish the portion of a PFC which the airlines may retain to reimburse them for their necessary and reasonable expenses in collecting and handling the fees.”

American Airlines requests that based on the evidence submitted by the air carriers, that this portion be increased to cover those costs of the carriers that are directly associated with collecting, handling, remitting, reporting, record keeping, and auditing of PFC's.

Sincerely,



Robin Campbell
Manager, Revenue Accounting
Sales and Tax Accounting
American Airlines

Enclosures

Note: The cost data and cost definitions contained in this submission are privileged and confidential information and protected from disclosure. If the reader of this information is not the intended recipient, or an agent responsible for delivering this information to the intended recipient, you are hereby notified that any dissemination, distribution, or copying of this communication is strictly prohibited.

Independent Accountants' Report on Applying Agreed-Upon Procedures

The Board of Directors and Management
American Airlines, Inc.
and
The Federal Aviation Administration

We have performed the procedures enumerated below, which were agreed to by American Airlines, Inc. (American Airlines or the Company) and the Federal Aviation Administration (FAA), solely to assist you in evaluating the accompanying schedule of incremental costs directly associated with Passenger Facility Charge (PFC) collection, handling, remittance, reporting, recordkeeping, and auditing for the year ended December 31, 1999. These incremental costs are presented in Exhibit I, American Airlines, Inc. Summary of Passenger Facility Charge Incremental Costs for the year ended December 31, 1999 (hereafter referred to as Exhibit I). This engagement to apply agreed-upon procedures was performed in accordance with standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of the FAA and the Company. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

It should be understood that certain of the schedules and/or analyses provided to us by the Company calculated incremental costs directly associated with PFCs based on assumptions and/or studies performed by the Company. Accordingly, we make no comment as to the reasonableness of the assumptions or as to the methodology underlying the studies.

The following procedures were performed with no exceptions noted:

1. We obtained Exhibit I from American Airlines of all costs attributed to the collection and administration of PFCs, by expense caption, for the year ended December 31, 1999.
2. We obtained a schedule from American Airlines of the total dollar amount and number of PFCs collected, refunded, and remitted for the year ended December 31, 1999 and agreed the total to an American Airlines system-generated report. We recalculated the number of PFCs collected for the year by dividing the total dollar amount of PFCs collected by \$3.
3. We obtained a schedule from American Airlines of the total dollar amount of interest income earned by the Company on PFC funds it held from the time of collection from passengers to the time of remittance to the airports (or the refund of the PFC funds to passengers) for the year ended December 31, 1999.

4. We recalculated Total Costs, Total Costs Less Interest, Cost Less Interest/PFC Remitted, and Cost Less Interest/PFC Collected appearing in Exhibit I.
5. We performed the following procedures related to each expense caption appearing in Exhibit I and the interest income earned amount as reported on the schedule obtained in step 3. And appearing in Exhibit I, for the year ended December 31, 1999:

Cost Caption

Procedures

- | | |
|---------------------|--|
| a. Credit Card Fees | <ol style="list-style-type: none"> i. We obtained from American Airlines a schedule containing the breakout of total revenue by month, for the year ended December 31, 1999, separated between credit card revenue and other revenue, and agreed two months of revenue (April 1999 and August 1999) to the general ledger. ii. We recalculated, based on the schedule obtained in step 5.a.i., the percentage of credit card revenue as a portion of total revenue for each month of 1999. iii. We recalculated the amount set forth on the schedule obtained in step 5.a.i. as PFC dollars collected via credit card sales for the year ended December 31, 1999 by multiplying total PFC dollars collected less PFC dollars refunded, from the schedule obtained in step 2., by the percentage calculated in step 5.a.ii for each month of 1999. iv. We recalculated the amount set forth on the schedule obtained in step 5.a.i. as credit card discount expense related to PFCs for the year ended December 31, 1999 by multiplying the "PFC dollars collected via credit card sales", as calculated in step 5.a.iii., by the average credit card discount percentage, as determined by American Airlines. v. We recalculated the amount set forth on the schedule obtained in step 5.a.i. as bad debt expense related to PFCs for the year ended December 31, 1999 using American Airlines' methodology and assumptions, which considered, among other things, credit card charge backs, return check expense, average fare and average PFC collection per ticket. vi. We summed the credit card discount expense, calculated in step 5.a.iv., and the bad debt expense, calculated in step 5.a.v., for the year ended December 31, 1999 and agreed the total to the respective amount appearing in Exhibit I. |
|---------------------|--|

- b. Audit Fees (External)
- i. We agreed the audit fees appearing in Exhibit I to the Ernst & Young schedule of fees for the PFC related audit, examination, and agreed-upon procedures for the year ended December 31, 1999.
- c. Disclosure Costs
- i. We obtained from American Airlines a summary of all disclosure cost components related to PFCs for the year ended December 31, 1999.
 - ii. We agreed the total costs from the schedule obtained in step 5.c.i. to the respective amount appearing in Exhibit I.
 - iii. We recalculated disclosure costs for the year ended December 31, 1999, using American Airlines' methodology and assumptions, which considered, among other things, the number of media units containing PFC information and cost per media unit attributed to disclosure.
- d. Reservations
- i. We obtained from American Airlines a summary of all reservation cost components related to PFCs for the year ended December 31, 1999.
 - ii. We agreed the total costs from the schedule obtained in step 5.d.i. to the respective amount appearing in Exhibit I.
 - iii. We recalculated reservations expense for the year ended December 31, 1999, using American Airlines' methodology and assumptions, which considered, among other things, total bookings, additional conversation time to state PFC applicability, average wage rate per hour and communications cost per second.
- e. Revenue Accounting and Accounts Payable
- Data Entry*
- i. We obtained from American Airlines a summary of all data entry cost components related to PFCs for the year ended December 31, 1999.
 - ii. We agreed the total costs from the schedule obtained in step 5.e.i. to the respective amount appearing in Exhibit I.
 - iii. We recalculated the data entry costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions which considered, among other things, total keystrokes, PFC keystrokes and cost per keystroke.
- Revenue Accounting*
- iv. We obtained from American Airlines a summary of all revenue accounting cost components related to PFCs for the year ended December 31, 1999.

- v. We agreed the total costs from the schedule obtained in step 5.e.iv. to the respective amount appearing in Exhibit I.
- vi. We recalculated the revenue accounting costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, estimates of managerial, staff, and clerical employee time spent related to PFCs and wage rates for the respective staff.

Accounts Payable

- vii. We obtained from American Airlines a summary of all accounts payable cost components related to PFCs for the year ended December 31, 1999.
- viii. We agreed the total costs from the schedule obtained in step 5.e.vii. to the respective amount appearing in Exhibit I.
- ix. We recalculated the accounts payable costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, December 31, which considered, among other things, estimates of data input time, monthly and quarterly mailings, and other costs related to PFC administration.

Tax

- x. We obtained from American Airlines a summary of all tax department cost components related to PFC's for the year ended December 31, 1999.
- xi. We agreed the total costs from the schedule obtained in step 5.e.x. to the respective amount appearing in Exhibit I.
- xii. We recalculated the tax costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, estimates of managerial, staff and clerical employee time spent related to PFCs and wage rates for the respective staff.

f. Corporate
Property

- i. We obtained from American Airlines a summary of all corporate property cost components related to PFCs for the year ended December 31, 1999.
- ii. We agreed the total costs from the schedule obtained in step 5.f.i. to the respective amount appearing in Exhibit I.

- iii. We recalculated the costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, estimates of employee time spent meeting with airports regarding PFCs and wage rates for the respective staff.

- g. Training: Reservations and Passenger Service Departments
 - i. We obtained from American Airlines a summary of all reservations and passenger service department training costs allocated to PFCs for the year ended December 31, 1999.
 - ii. We agreed the total costs from the schedule obtained in step 5.g.i. to the respective amounts appearing in Exhibit I.
 - iii. We recalculated the costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, number of agents trained, minutes to train on PFC related subjects and cost per training minute.

- h. Carrier On-Going Information Systems
 - i. We obtained from American Airlines a summary of all carrier ongoing information systems costs allocated to PFCs for the year ended December 31, 1999.
 - ii. We agreed the total costs from the schedule obtained in step 5.h.i. to the respective amount appearing in Exhibit I.
 - iii. We recalculated the costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, ongoing costs related to data storage and amount of data storage related to PFCs.

- i. CRS On-Going Costs
 - i. We obtained from American Airlines a summary of all costs related to ongoing maintenance of PFC data for the year ended December 31, 1999.
 - ii. We agreed the total cost from the schedule obtained step 5.i.i. to the respective amount appearing in Exhibit I.
 - iii. We recalculated the costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, booking fees and the proportion of booking fees attributable to maintaining PFC data.

- j. Airline Tariff Publishing Company (ATPCO)
 - i. We obtained from American Airlines a schedule of all ATPCO costs allocated to PFCs for the year ended December 31, 1999.
 - ii. We agreed the total costs from the schedule obtained in step 5.j.i. to the respective amount appearing in Exhibit I.

- iii. We recalculated the costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, total PFC processing costs for ATPCO and American Airlines' percentage of ATPCO business.
- k. Airline Reporting Corporation (ARC)
 - i. We obtained from American Airlines a schedule of all ARC costs attributed to PFCs for the year ended December 31, 1999.
 - ii. We agreed the total costs from the schedule obtained in step 5.k.i. to the respective amount appearing in Exhibit I.
 - iii. We recalculated the costs for the year ended December 31, 1999, based on American Airlines' methodology and assumptions, which considered, among other things, American Airlines' charges from ARC and the proportion of those charges considered to be incremental due to PFCs.
 - iv. We selected the five largest charges to American Airlines from ARC for the year ended December 31, 1999 detailed on the schedule obtained in step 5.k.i. and agreed the charges to the respective ARC invoice (or other document supporting such costs).
- l. Interest Income
 - i. We obtained from American Airlines a schedule containing the breakout of the total dollar amount of interest earned on PFC funds held by the Company by month, for the year ended December 31, 1999.
 - ii. We obtained from American Airlines a schedule showing the average number of days that a PFC collected in each month was held from time of receipt by the airline to the time of remittance to the airports or, in the case of refunded tickets, time of refund to the passenger.
 - iii. We obtained from American Airlines a schedule of the average interest rates earned for each month in 1999 on its short-term investment portfolio.
 - iv. We obtained a schedule of Interest earned on PFC dollars collected from sales for the year ended December 31, 1999 and we recalculated two months (February 1999 and November 1999) by multiplying monthly PFC dollars collected from the schedule obtained in step 2. by days held (both for remitted PFCs and PFCs refunded to passengers) as a proportion of a 365-day year obtained in step 5.l.ii., and then by the appropriate monthly interest rate percentages obtained in step 5.l.iii.
 - v. We agreed the total of Interest earned on PFC dollars collected from sales appearing in the schedule obtained in step 5.l.iv. for each month to the respective amount reported in the schedule obtained in step 3. and appearing in Exhibit I.

We were not engaged to, and did not, perform an audit, the objective of which would be the expression of an opinion on the accompanying Summary of Passenger Facility Charge Incremental Costs of American Airlines, Inc. for the year ended December 31, 1999. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the Board of Directors and management of the Company and the FAA, and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of the procedures for their purposes. However, this restriction is not intended to limit the distribution of this report, which is a matter of public record.

Very truly yours,

Ernst + Young LLP

December 19, 2000

EXHIBIT I

American Airlines, Inc.
 Summary of PFC Incremental Costs
 For the Year Ended December 31, 1999
 (See Note 1)

	1999 <u>Actual Costs</u>
Credit Card Fees	\$3,602,318
Audit Fees (External)	41,650
Disclosure Costs	12,000
Reservations	2,744,990
Revenue Accounting and Accounts Payable:	
Data Entry	21,122
Revenue Accounting	218,614
Accounts Payable	3,042
Tax	38,739
Corporate Property Department	34,715
Training:	
Passenger Service (Ticket Agents)	232,238
Reservations	6,064
Carrier On-Going Information Systems	44,812
CRS On-Going Costs	1,359,659
PFC Absorption	-
Airline Tariff Publishing Company (ATPCO)	2,542
Airline Reporting Corporation (ARC)	<u>166,818</u>
 TOTAL COSTS	 8,529,323
 Interest Income Earned on Float	 <u>(1,333,915)</u>
 TOTAL COSTS LESS INTEREST	 <u><u>\$7,195,407</u></u>
 Number of PFCs Remitted	 66,370,574
Number of PFCs Collected	72,102,507
 Cost Less Interest / PFC Remitted	 \$0.1084
 Cost Less Interest / PFC Collected	 \$0.0998

Note 1: The amounts appearing on this Exhibit have been determined in accordance with the cost definitions and methodologies set forth in the PFC Incremental Cost Definitions provided by the Federal Aviation Administration (FAA) to American Airlines, Inc. (American) and certain other airlines in its letter dated October 19, 2000, as revised by American. Such revised cost definitions and methodologies are described by American in an attachment to its submission of Passenger Facility Charge Incremental Cost Data to the FAA on December 29, 2000.

**Airline, Inc. Summary Table
(1999 Actual, 2000-2002 Forecast)**

	1999 Actual Costs ¹		1999 Pro-Forma ²		Implementation	2000* Actual Costs		Full Year Costs		2000 (11 Act.+ 1		Forecast 2001 ^{5,6}		Forecast 2002 ^{5,7}	
					Costs ³	for 11 Months	Fore.) ^{4,5}	Forecast 2001 ^{5,6}	Forecast 2002 ^{5,7}						
Credit Card Fees	\$3,602,318	42%	\$4,875,624	50%		3,792,030	44%	\$4,134,510	\$5,175,084	6,673,068					
Audit Fees (External)	\$41,650	0%	41,650	0%	31,182	41,650	0%	41,650	41,650	41,650					
Disclosure Costs	\$12,000	0%	12,000	0%		12,000	0%	12,000	12,000	12,000					
Reservations	\$2,744,990	32%	2,744,990	28%		2,724,129	31%	\$2,823,458	2,843,703	2,898,862					
Passenger Services	\$0	0%	-	0%		-	0%	-	-	-					
Data Entry:															
Internal	\$21,122	0%	21,122	0%		10,559	0%	\$10,559	5,496	2,996					
Other	-	0%	-	0%		-	0%	-	-	-					
Staffing:															
Revenue Accounting	\$218,614	3%	218,614	2%		233,434	3%	233,434	263,561	291,802					
Accounts Payable	\$3,042	0%	3,042	0%		\$3,066	0%	\$3,066	3,140	3,218					
Tax & Legal	\$38,739	0%	38,739	0%		38,739	0%	38,739	41,900	43,576					
Corporate Property Department	\$34,715	0%	34,715	0%		\$34,715	0%	\$34,715	\$37,548	\$39,050					
Training:															
Reservations	\$6,064	0%	6,064	0%		158	0%	158	-	-					
Other	-	0%	-	0%		-	0%	-	-	-					
Ticket Agents	\$232,238	3%	232,238	2%		273,936	3%	273,936	281,719	281,719					
Internal On-Going IT	\$44,812	1%	44,812	0%		37,822	0%	39,067	37,208	35,751					
CRS On-Going fees	\$1,359,659	16%	1,359,659	14%		1,349,827	16%	\$1,431,495	1,527,858	1,624,220					
PFC Absorption	-	0%	-	0%		-	0%	-	-	-					
ATPCO	\$2,542	0%	2,542	0%	0%	2,542	0%	2,542	2,542	2,542					
ARC + BSP	\$166,818	2%	166,818	2%	0%	165,394	2%	175,412	179,104	182,905					
Internal One-Time IT update	-	0%	-	0%	329,403	-	0%	-	-	-					
CRS One-Time update	-	0%	-	0%		-	0%	-	-	-					
Interest Revenue on Float	(\$1,333,915)	n/a	(\$1,985,704)	n/a		(1,592,149)	n/a	(1,737,001)	(2,158,018)	(2,786,883)					
TOTAL COSTS	8,529,323	100%	9,802,630	100%	360,585	8,685,286	100%	9,220,026	10,414,965	12,094,309					
TOTAL COSTS LESS INTEREST	7,195,407	n/a	7,816,926	n/a	360,585	7,093,137	n/a	7,483,025	8,256,947	9,307,426					
Number of PFCs Remitted	66,370,574		66,370,574		66,370,574	66,292,863		72,319,487	73,765,877	75,241,194					
Number of PFCs Collected	72,102,507		72,102,507		72,102,507	72,002,851		78,548,565	80,119,536	81,721,927					

Not included in total

Cost Less Interest / PFC Remitted	\$0.1084	\$0.1178	\$0.0054	\$0.1070	\$0.1035	\$0.1119	\$0.1237
YOY Change				-1.3%	-3.3%	8.2%	10.5%

Cost Less Interest / PFC Collected	\$0.0998	\$0.1084	\$0.0050	\$0.0985	\$0.0953	\$0.1031	\$0.1139
YOY Change				-1.3%	-3.3%	8.2%	10.5%

Airline, Inc. Specific Issue	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Cost Less Interest / PFC Remitted	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000
Cost Less Interest / PFC Collected	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000

Airline, Inc. Specific Issue	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Cost Less Interest / PFC Remitted	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000
Cost Less Interest / PFC Collected	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000	\$0.000

ASM growth rate					2.0%	2.0%	2.0%
CPI - Urban from WEFA ⁸					3.3%	2.4%	2.4%

Notes:
1 - Actual costs incurred. Agreed upon procedures have been applied by the independent accountant to actual 1999 costs.
2 - Assumes the same volume as 1999, but with 100% of PFCs Collected at \$4.50 per PFC – this only impacts Credit Card Fees and Interest Revenue.
3 - For any costs associated with the implementation of the new maximum \$4.50 PFC rate. This column is not year specific.
4 - (X) months of 2000 are actual with (Y) months of forecast.
5 - Does not include any one time IT Costs (Implementation Costs).
6 - Assumes 3 months with 100% of PFCs Collected at \$3. Assumes 9 months with 50% at \$3 and 50% at \$4.50.
7 - Assumes 12 months with 100% of PFCs at \$4.50.
8 - WEFA US Economic Outlook 2000-05 - US Cycle Monitor, September 2000, page 201. All Items - Urban Wage Earners. Application of an inflation index or other index will be evaluated in the rulemaking process and, if allowed, may apply only to selected cost components (e.g., labor costs). Please indicate which cost components have been adjusted by the specified CPI or other index and why.

American Airlines, Inc.,
Attachment I
PFC Cost Analysis Assumptions

- a. Credit card fees – AA separated revenue into cash and credit card form of payment to determine the percentage of credit card sales. This percentage was used with an average credit card discount percentage to determine the cost associated with a \$3 level of collection along with a \$4.50 level of collection. This amount was added to the Bad Debt Expense attributed to PFC's. The PFC Bad Debt was determined by multiplying the bad debt rate by PFC's collected on credit.
- b. Audit fees – Ernst and Young provided this information based on 1999 billings to airline.
- c. PFC Disclosure – AA assumed no media advertising in 1999 that required PFC disclosure. However, based on information from the Marketing department, AA did assume a small percentage of disclosure costs related to aa.com advertising where PFC disclosure is required.
- d. Reservations – AA utilized an estimate provided by Domestic Reservations of calls involving a fare quote that included a PFC. AA assumed six seconds are required to explain PFC Revenue to passengers. This information was extrapolated across average segments per booking and passengers per record.
- e. Passenger Service – N/A
- f. Revenue Accounting, Data Entry, Accounts Payable and Tax – AA determined personnel in each of these departments whose job involves PFC's. Revenue Accounting has staff dedicated specifically to PFC's while the other departments have other responsibilities. AA obtained the average salaries for the levels involved and percentage of time spent with PFC collections and remittances.
- g. Corporate Property – AA obtained the average salaries for the levels involved and percentage of time spent with PFC collections and remittances.
- h. Training—Reservations, Ticket Agents and Other Departments – Flagship University offers to agents (Reservations and Ticketing) a specific PFC class. The actual class cost was applied to the number of students that attended this class in 1999. A percentage of Instructor time was included.

- i. Carrier Ongoing Information Systems – Actual invoices were used to determine 1999 maintenance costs, storage costs and monthly processing costs based on volume of PFC's.
- j. CRS Ongoing Costs – CRS's provide PFC information that is used for ticketing purposes. All ticketing services are billed as Booking fees. AA assumed a very small percentage of Booking fees attributable to PFC costs.
- k. PFC Absorption – N/A
- l. Airline Tariff Publishing Company (ATPCO) – ATPCO provided to each carrier their costs that relate solely to PFC's.
- m. Airline Reporting Corporation (ARC) and Billing Settlement Plans (BSP) – AA determined the percentage of keystrokes related to PFC's to determine the PFC-related cost of processing and storage from these two sales sources.
- n. Interest Income – AA used net remitted with a 1-½ month float at an average short-term interest rate.