BEFORE THE
FEDERAL AVIATION ADMINISTRATION
WASHINGTON, DC

In the matter of	)	
	)	
Procedures for Reimbursement of Airports,	)	
On-Airport Parking Lots and Vendors	)	**Docket FAA-2001-11172**
of On-Airfield Direct Services to	)	
Air Carriers for Security Mandates	)	
	)	
14 CFR Part 154, Notice No. 154	)	

COMMENTS OF SKY CHEFS, INC.

Communications with regard to this documents should be sent to:

Diane Emanuel
Senior Director Security
Sky Chefs, Inc.
524 E. Lamar Boulevard
Arlington, TX 76011

J.E. Murdock III
SHAW PITTMAN
2300 N Street, N.W.
Washington, D.C. 20037
(202) 663-8342
sandy.murdock@shawpittman.com

Dated: January 22, 2002

BEFORE THE
FEDERAL AVIATION ADMINISTRATION
WASHINGTON, DC

In the matter of	)	
	)	
Procedures for Reimbursement of Airports,	)	
On-Airport Parking Lots and Vendors	)	**Docket FAA-2001-11172**
of On-Airfield Direct Services to	)	
Air Carriers for Security Mandates	)	
	)	
14 CFR Part 154, Notice No. 154	)	

COMMENTS
OF
SKY CHEFS, INC.

By Notice of Proposed Rule Making (NPRM), dated December 21, 2001, the Federal Aviation Administration (FAA) proposed procedures for reimbursement for Airports, Airport Parking Lot Operators, and Vendors of "on-airfield direct services to air carriers" (Vendors). These comments are submitted in response thereto on behalf of Sky Chefs, Inc. ("Sky Chefs"), d/b/a LSG Sky Chefs.

Section 121 of the Aviation and Transportation Security Act (ATSA) authorized the FAA to reimburse airports, airport parking lot operators, and vendors for certain costs associated with the increased security measures implemented after September 11, 2001. That statute did not appropriate the $1.5 billion authorized therein. Supplemental legislation has appropriated funds for the reimbursement of airports. While there is no legislation pending that would appropriate funds for vendors, several Members of Congress have committed to introducing and supporting such legislation.

Sky Chefs is one of the largest providers of food services to airlines. It has over 80 facilities, primarily kitchens, at airports around the country. The company had devoted substantial time and money to comply with the FAA security requirements before September 11; after that date there was a quantum increase in the assets expended to meet the new requirements. It is important to note that the added expenses included the acquisition of what it believes were and are capital assets, prerequisites for compliance.

Sky Chefs does not hold a FAA certificate; consequently, it is not privy to FAA security directives, plans or amendments thereof under 14 CFR Part 107 and 108.[1] Sky Chefs is authorized to be on the airport by virtue either of its status as an airline vendor (the carrier provides the Part 108 authorization for access of the SIDA) at many airports or as an airport tenant (the airport issues the SIDA badges under Part 107) at some airports. Thus, when the FAA changes the security regime, Sky Chefs does not receive the FAA's new directive directly, but must rely on the information communicated to it by

[1] "Security directives, emergency amendments, orders, regulation approved airport and air carrier security programs, contingency measures and implementing instructions" are the FAA's full list of possible documents monitored by the FAA that may communicate the agency's security requirements. These comments, for brevity purposes, will not repeat this litany every time that

Footnote continued on next page

the airline and/or the airport. Particularly as to the transmission of information by the airline, which is their customer at every airport the company serves, the source of information about the new FAA position or interpretation is not the airline security organization. Rather the Sky Chefs staff person, who works directly with each airline, usually communicates with someone in the contract administration or food services organization. The Security Directives that the company receives are almost never a hard copy of the FAA most recently issued paper, but rather, typically are orally conveyed. That airline direction may include its interpretation of the FAA requirements and may well include the airline's policy developed in response to an FAA directive. The policy may, and frequently does, incorporate additional procedures or paperwork or specific requirements that were not specifically required in the FAA paper.

Below are the comments of Sky Chefs on the FAA NPRM:

1. <u>§154.3-Definitions Should Include the "Search and Seal" Function.</u>

The definition of "direct air services to an air carrier", found in the NPRM preamble, includes an extensive list. It, however, does not mention the one function that was 100% mandated by an FAA Security Directive issued after September 11, 2001.

Footnote continued from previous page

reference is made to some FAA mandate; however, we request that the FAA assume that the full list be considered as appropriate.

Prior to that date there was no “search and seal” function, see Security Directive 108-01-10D, nor was there a requirement that a “search and seal” organization be independent of the food services company. Out of an abundance of caution, the preamble to the Final Rule should include the “search and seal” function in its recitation. Clearly Congress intended to include security requirements imposed after September 11; Security Directive 108-01-10D was issued on October 18, 2001, the mandated requirements should be included.

The impact on Sky Chefs of the “search and seal” directive had several different direct impacts. The time that it takes to move a food tray or cart through one of our kitchens, for example, increased. After the new SD, time was allotted to perform the search and seal step before the food was loaded on the truck. Another impact of this new requirement was the breaking of the seal at planeside; additional time was required to have the airline representative match the seal number against the number assigned at the kitchen. A seemingly simple operation, however, was made more complex when applied in reality. Catering trucks typically service more than one airplane on a single trip. Under the interpretation of some airlines, once the seal attached to the truck was broken, a second inspection and a new number were required. These steps added up quickly and raised the cost of doing business under this SD. There are further examples of how the SD affected our business.

2. §154.3-Definitions "On the Airfield" Should be Clarified.

The "on the airfield" definition indicates that the service, to be eligible, should be delivered in the Airport Operating Area ("AOA"). The clarifying comment suggests that the facility need not be an airport, "so long as the work is performed on the airfield." The example of the repair of an aircraft indicates that "at least part of the service [must] be on the airfield to be covered." Sky Chefs appears to meet this test; its facilities (mostly kitchens) are located both on airport and off airport, but the food is always delivered directly to the aircraft in the AOA. Thus, all of its added mandated security costs should be eligible.

The preamble to the final rate should, we request, mention this example.

3. §154.3 – Definition- "Eligible Security Requirements" are difficult for Vendors to know.

It is a very common phenomena for a company like Sky Chefs to receive a call from a customer airline and to be told that, under the FAA security plan, "all your trucks need to be padlocked". Because under Part 191 the company does not have direct access to the FAA protected documents, the company complied with the airline requirement under the assumption that the requirement was issued by the FAA.

We do not and cannot know whether the FAA mandated the "padlock" through a Security Directive or some other Part 107 or 108 mandate. We do not and cannot know whether the air carrier included the "padlock" requirement as part of its FAA approved plan, or under its interpretation of what an FAA SD required, or through its individual decision that a padlock rule was authorized under its exercise of its air carrier certificate obligations, without a further FAA directive. All that is clear is that the vendor must do what it was instructed to do by the airline.

In that the company has contracts with many airlines, one might assume that, soon after a new SD or other FAA mandate is issued, Sky Chefs would learn from the airlines the precise FAA guidance to its vendors. That is not the case. Whether the PSIs provide slightly different interpretations at the first step in the information chain; or whether the individual airlines, through their own process, randomly create variations in the interpretation; or whether the simple process of each airline's interpreting how to apply the FAA directive intentionally creates differing practical instructions; or whether the differing messages are the result of the variations caused by our employee's listening skills; a typical FAA SD initiative results in a wide range of specific airline instructions.

This NPRM No. 154 assumes that the vendors receive clear, precise instructions as to what the FAA mandates are and that the vendors can readily discern what the FAA "eligible security requirements" are. This is not so.

One final example of why there may be confusion as to what constitutes an eligible expense. One or more airlines communicated to Sky Chefs that the "perimeter" of their on-airport facility must be secure. It was assumed that the language came from the FAA. Based on those airline instructions of what purported to be an FAA SD, Sky Chefs felt obligated to hire guards to "secure" each access point to its kitchens. It also was believed that such a security measure should be applied whether the kitchen was on airfield or off the airport premises. The rationale was that contraband could be introduced at either type of site and that the transfer of weapons, etc. from the kitchen, wherever located, would pose an equal threat. In response to such an airline directive, the companies have implemented expensive procedures under the honest belief that the FAA mandated the resulting action.

Based on these observations, the FAA should allow the vendor to exercise its best judgment as to what may have been required and have the FAA determine what is eligible.

If the FAA adopts this approach, the certification (§154.17, §154.19 and Appendix A) should be modified to reflect the reality that neither the company can provide a certificate (§ 154.19) nor could an auditor (§ 154.23) certify that the expenses claim meet the eligibility requirements of Part 154. Under Part 191 neither the company nor the auditor can have access to the restricted information.

One final point should be made; the concept about an applicant must submit an audit by an outside accountant fails to recognize the purpose of § 121 of ATSA. Companies have been burdened by extraordinary expenses; Congress has decided that these companies need financial relief; to require an additional outside audit adds to the very expenses Congress was trying to reimburse! The final rule should not require an audit provided by an outside accountant.

4. <u>§154.13 – Distribution: The Application Due Date Should be Amended</u>

Congress has taken exceptional action in authorizing this reimbursement regime. It is unusual for the House, Senate and Administration to agree that private companies should be compensated for regulatorily-mandated expenses. This legislation was enacted, we would argue, because Congress acknowledged that these security measures were extraordinary and that the companies bearing these costs have been negatively impacted to an extreme degree. The expenses at issue have been incurred over the past almost five months, will continue to accumulate until a final rule is issued and will not be offset by any reimbursement until the federal government issues a check under ATSA and appropriation legislation. In the interim each eligible company is financing significant operational and capital expenses; those on-going obligations are producing massive financial pressures on the vendor companies. There is much urgency to the recompense of these expenses; the choice of an application date of June 1, 2002 does not reflect the extreme need for immediate relief.

There is no practical reason to wait until June to submit the request for reimbursement. Each vendor believes that it knows now what the dollar amounts of these added security requirements are and will continue to be. Many of the FAA mandates have been in place since September and October; as best we can tell, few new FAA requirements have been imposed on the vendors recently. The Final Rule should require the vendor to submit their applications on March 1, 2002, because the necessary supporting information is available today. An extra three months is not required for the vendors to prepare full, substantiated and accurate applications.

If the FAA and/or TSA makes changes to the requirements applicable to vendors between now and the due date or after the due date, the vendors would be willing to amend their requests for reimbursement. Given the recent lack of activity, such security changes are not foreseeable.

Many vendors desperately need these funds. The final rule should be amended to move up the date from June 1, 2002 to March 1, 2002. Although the appropriations legislation has not been enacted, there are several good reasons to advance the due date:

(i) the calculation of the actual total vendor reimbursement needs will facilitate Congress's passage of an appropriation bill;

(ii) the time between the deadline and Congressional enactment can be used to audit the vendor application data; and

(iii) the June 1 date bears no greater relationship to the appropriations process; typically these bills are not passed by that date; however by March, the Administration's proposed appropriations bill has usually been circulated

> and the Congressional hearings (particularly those relevant to the appropriations legislation) have been usually completed by that date.

We would urge that the final rule adopt as the application date, March 1, 2002 to reflect the urgency of the situation. Private lenders will regard such an action as some indication that relief may be forthcoming.

5. § 154.7 Distribution – Pro Rata Does Not Reflect the Individual Degree of Economic Impact.

The vendors, parking lot operators and airports (we assume that the airports have been redressed in the supplemental appropriation and are not truly at issue here) have all been substantially impacted by the FAA mandates. Many airline vendors have had cost increases of substantial percentages and revenue decreases of equal or greater proportions. Many parking lot operators have seen their revenues go to zero, while others have not had the same negative economic impact. Their cost impacts have also varied based on the proximity of their parking lots to the terminal. The same wide variations in both revenues and costs are likely among airports. The statute, however, only recognizes added expenses; the net financial impact was ignored by Congress' word choice. That drafting decision to examine only expenses should not preclude the FAA's consideration of the range of comparative impact.

A pro rata distribution fails to recognize any such relative equity. Very large institutions, public or private, have greater financial reserves than a small business would have available. For a marginally capitalized entity, loss of income or increase in costs of even a small percentage can put the enterprise at risk. A purely pro rata distribution rule fails to recognize such comparative impacts. A very large company or airport may experience increased costs in the millions with a revenue base in the billions. Such entities do not need the same level of financial assistance as a smaller, less secure firm. Under the NPRM proposed formula a very large entity with very large, (in absolute dollar terms), expenses will receive a higher percentage of a pro rata distributions than a smaller airport/business with smaller absolute dollar impacts, even though the latter category may have experienced a greater negative impact and may be at greater risk.

The NPRM's pro rata proposal should be amended to reflect some level of equity. Firms should be required to show the eligible expenses as a percentage of the actual revenues during the relevant period. This percentage would reflect a degree of impact and should help create a prioritization for the distribution. The recompensation basis should not be purely as to percentage, but the severity of the impact and absolute dollar amount both should be considered.

6. § 154.7 Distribution – Ten Percent Withholding is an Unnecessary Protection

The NPRM again seems to fail to recognize the financial exigencies that the vendors have experienced and continue to experience as a result of these added rules.

Many of the vendors at issue are financially strapped. By withholding ten percent of its reimbursement, the FAA may be denying companies much needed cash. The need for compensation is immediate. The need to protect the ten percent by withholding is neither justified nor the most efficient method of controlling this money.

Today the federal government pays and receives billions of dollars in grants and taxes without withholding. The FAA's own AIP program issues billions of dollars in grant money without retaining some percentage. The expenses here at issue are capable of reliable proof and will be subjected to audit. Payment of the full application amount, subject to audit and refund, is appropriate given the urgency of the situation, the degree to which the government can audit "direct costs" and the relatively small number of companies that are eligible and likely to seek compensation.

7. <u>§154.9 Reimbursement Limits – Relevant Capital Costs must be Included</u>

Many of the FAA directives resulted in substantial capital expenditures; fingerprinting equipment, new security systems, etc. are primary examples of the major impact of the new security regime. The NPRM seems to exclude such relevant costs from consideration. While perhaps an expense, which has an expected life of greater than one year should not be fully recognized, the FAA must acknowledge the validity of these agency-mandated expenses through some amortization rule. The acquisition of new capital assets was among the most burdensome expenses imposed as a result of

September 11, 2001. An accounting system, which ignores such capital expenses, which fails to reflect the real financial impact of the FAA's actions, which distorts recovery among the various applicants (some companies were required to acquire more assets than others) and which is not required by ATSA, does not seem to be well advised. Equity can be restored, if the final rule incorporates a reasonable amortization procedure which allows the applicant to include the financial impact of such capital expenditures for the relevant period.

8. § 154.17 – Reimbursement Proof

Documents clearly labeled as directly related to a specific expense are not required under most accounting procedures. While ideally there are records which solely relate to specific, new security expense, such documentation is not required for an accountant to make reasonable, substantiated cost allocations. The NPRM seems to suggest that each vendor opened up a new ledger in the midst of the September 11 crisis and neatly entered each new security expense. That is not realistic.

What did happen was management made a series of quick decisions attempting to implement the FAA mandated requirements as soon as possible. Equipment was purchased, procedures were designed by consultants, fingerprint firms were hired and a whole host of urgent actions were taken to comply with the FAA rules.

Many expenses increased without any specific accounting entry. One of the clearest and most direct expenses incurred by Sky Chefs was the added time required to move its food from its kitchens to the aircraft. The Sky Chefs financial systems track the time that their trucks require to move the food from the kitchens to the airplanes. That analysis shows that the time spent daily during this period increased. It is clear that this added time and costs were created by the increased, FAA mandated time spent at airport access points while our trucks' contents and the contents of other vehicles were examined by airport security personnel under the new Security Directives. These added expenses are dramatic; our accounting organization can demonstrate the precise burden of the new security measures through standard procedures.

Some of theses expenses were recorded as a line item in a bill, some were included in existing service or supply contracts and reflected as added total costs; and others can be deduced through tested accounting procedures. The final rule should acknowledge that statements by accountants, based on careful reviews, will be accepted if the underlying financial analysis is supported by standards, normal accounting procedures and adequate documentation. To require ledger-like proof is to deny the reality of the situation and to reward the institution with the most fastidious accountants. The final rule should provide more latitude.

9. <u>§ 154.9 Reimbursement Limits – Offsetting of Surcharges, Fees, etc.</u>

The NPRM suggest that if the applicant imposed a surcharge or fee, “the costs would not be reimbursed.” The language of the NPRM is not so precise; consequently this interpretation may be extreme. A more appropriate statement would appear to be “to the extent that such surcharge or fees exceed costs, then those costs would not be reimbursed.”

The economics of this situation are complex. First, the vendors incurred costs beginning on some specific date(s). The added fees or surcharges were imposed days if not weeks, after the expenses were incurred. The added revenues were not collected until weeks, or months after the expenses were paid. This delay factor means that the vendor had to finance the expenses, until (when and if) the added revenues equaled the actual expenses. At a minimum this delay phenomena should recognize the interest expense related to this situation. Second, it is unlikely that the vendor was able to impose a fee that truly compensated the company for all of the related costs.

While the NPRM considers only the expense aspect of the situation, the surcharge of a fee may have been assessed by the vendor in order to recover indirect costs, financial expenses, lost revenues, penalties imposed through contract cancellation, personnel costs associated with laying off staff, etc. These all constitute valid business reasons for imposing a fee. The company or companies that successfully implemented such fees should not be penalized if the dollars it received under such surcharge exceeded its eligible security costs. An applicant, that imposed a fee, should be allowed to demonstrate what cost targets were used to assess the fee and whether it was able to recover some or all of those costs. Any shortfall between targeted costs and actual recovery should translate to pro rata percentages among the various targets. To the extent that the eligible security target was greater that the apportioned revenues, the vendor should be able to claim that difference.

10. Summary

All of the above comments have been critical of the FAA NPRM. The nature of the process does not lend itself to detailed explanations of when the agency got it right. Much of the proposed rule is quite right. Given that the FAA was permitted an extraordinarily short period in which to draft complex rules for an ill-defined reimbursement statute, the staff should be commended. The comments provided here reflect strongly held concerns of companies that were impacted by September 11 and the FAA's subsequent security actions. Because these companies balance sheets and operations had concrete examples of impacts, they have unique and valuable insights as to how the NPRM affects each of them. Our comments are not meant to be critical, but intend to express real, substantial concerns. Primary to our response is the idea that the industry is hurting, that there is a sense of financial exigency and that we hope the final rule reflects such urgency.

WHEREFORE, for the above stated reasons, Sky Chefs requests that the FAA include the suggested changes in the final rule.

Respectfully submitted

/ s /

____

J.E. Murdock III

Counsel to
Sky Chefs, Inc.

DATED: January 22, 2002

CERTIFICATE OF SERVICE

I hereby certify that I have this 22 day of January, 2002, served the foregoing Comments of Sky Chefs below in accordance with the FAA's Rules.

Diane Giuliani