



CITY OF PHILADELPHIA

**Philadelphia Airport System
Municipal Securities Disclosure
Annual Financial Information
Fiscal Year Ended June 30, 2009**



**Philadelphia Airport System
Municipal Securities Disclosure
Annual Financial Information
Fiscal Year Ended June 30, 2009**

This report has been prepared pursuant to certain provisions of the following Continuing Disclosure Agreements, collectively referred to as the “Disclosure Agreements”:

- . Continuing Disclosure Agreements dated July 23, 1998 and July 10, 2001 between the Philadelphia Authority for Industrial Development and the City of Philadelphia, Pennsylvania
- . Continuing Disclosure Agreement dated July 10, 2001 between the City of Philadelphia, Pennsylvania and First Union National Bank
- . Continuing Disclosure Agreements dated June 1, 2005, August 4, 2005, August 1, 2007 and April 14, 2009 between the City of Philadelphia, Pennsylvania and Digital Assurance Certification, L.L.C.

This report contains the following financial information and operating data which, together with the City of Philadelphia’s Comprehensive Annual Financial Report (“CAFR”), constitute the “Annual Financial Information” as defined in the Disclosure Agreements:

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In accordance with Section 3 of the Disclosure Agreements, the above-referenced tables and appendix are substantially similar to the type set forth in the Official Statements for the Philadelphia Authority for Industrial Development Airport Revenue Bonds, Series 1998A and Series 2001A and the City of Philadelphia, Pennsylvania Airport Revenue Bonds, Series 2001B, 2005A, 2005C, 2007A/B and 2009A.

TABLE 1

**Philadelphia International Airport
Recent Trends in Enplaned Passengers
FY 2007 - FY 2010**

| <u>Airlines</u> | <u>FY 2007</u> | <u>FY 2008</u> | <u>Percent Increase (Decrease)</u> | <u>FY 2009</u> | <u>Percent Increase (Decrease)</u> | <u>First 6 Months (July - December)</u> | | |
|----------------------------------|-------------------|-------------------|--|-------------------|--|---|------------------|--|
| | | | | | | <u>FY 2009</u> | <u>FY 2010</u> | <u>Percent Increase (Decrease)</u> |
| Domestic | | | | | | | | |
| Scheduled Major / National | | | | | | | | |
| US Airways | 4,798,292 | 4,694,777 | -2.16% | 4,586,744 | -2.30% | 2,387,748 | 2,403,542 | 0.66% |
| Other | <u>5,349,519</u> | <u>5,309,353</u> | <u>-0.75%</u> | <u>4,692,202</u> | <u>-11.62%</u> | <u>2,516,095</u> | <u>2,272,365</u> | <u>-9.69%</u> |
| | 10,147,811 | 10,004,130 | -1.42% | 9,278,946 | -7.25% | 4,903,843 | 4,675,907 | -4.65% |
| Scheduled Regional / Commuter | 3,714,189 | 3,965,290 | 6.76% | 4,077,215 | 2.82% | 2,060,592 | 2,119,926 | 2.88% |
| Charter | <u>2,721</u> | <u>1,636</u> | <u>-39.88%</u> | <u>1,285</u> | <u>-21.45%</u> | <u>434</u> | <u>459</u> | <u>5.76%</u> |
| Subtotal - Domestic | 13,864,721 | 13,971,056 | 0.77% | 13,357,446 | -4.39% | 6,964,869 | 6,796,292 | -2.42% |
| International | | | | | | | | |
| Scheduled | 1,984,250 | 2,080,261 | 4.84% | 2,003,441 | -3.69% | 976,113 | 1,058,292 | 8.42% |
| Charter | <u>2,720</u> | <u>1,656</u> | <u>-39.12%</u> | <u>1,856</u> | <u>12.08%</u> | <u>343</u> | <u>0</u> | <u>-100.00%</u> |
| Subtotal - International | 1,986,970 | 2,081,917 | 4.78% | 2,005,297 | -3.68% | 976,456 | 1,058,292 | 8.38% |
| Total Enplaned Passengers | 15,851,691 | 16,052,973 | 1.27% | 15,362,743 | -4.30% | 7,941,325 | 7,854,584 | -1.09% |

Note: The City's Fiscal Year Ends June 30.

TABLE 2

**Philadelphia International Airport
Airline Market Shares of Enplaned Passengers
Fiscal Year 2009**

| <u>Airlines</u> | <u>Enplaned Passengers</u> | <u>Percent</u> |
|----------------------------------|----------------------------|----------------|
| Domestic | | |
| Scheduled Major / National | | |
| US Airways | 4,586,744 | 29.9% |
| Southwest | 1,895,701 | 12.3% |
| American | 606,551 | 3.9% |
| Delta | 571,723 | 3.7% |
| United | 538,269 | 3.5% |
| AirTran | 370,833 | 2.4% |
| Northwest | 337,432 | 2.2% |
| Continental | 234,198 | 1.5% |
| Frontier | 52,366 | 0.3% |
| Midwest | 50,384 | 0.3% |
| USA 3000 | <u>34,745</u> | <u>0.2%</u> |
| | 9,278,946 | 60.4% |
| Scheduled Regional / Commuter | | |
| US Airways Express | | |
| Republic | 1,396,362 | 9.1% |
| Air Wisconsin | 1,320,560 | 8.6% |
| Piedmont | 675,918 | 4.4% |
| PSA | 176,692 | 1.2% |
| Chautauqua | <u>62,312</u> | <u>0.4%</u> |
| | 3,631,844 | 23.6% |
| Other | <u>445,371</u> | <u>2.9%</u> |
| | 4,077,215 | 26.5% |
| Charter | <u>1,285</u> | <u>0.0%</u> |
| Subtotal - Domestic | 13,357,446 | 86.9% |
| International | | |
| Scheduled | | |
| US Airways | 1,558,766 | 10.1% |
| Air Wisconsin | 104,297 | 0.7% |
| British Airways | 103,473 | 0.7% |
| Lufthansa | 69,804 | 0.5% |
| Air France | 50,549 | 0.3% |
| Air Jamaica | 42,537 | 0.3% |
| Air Canada and Jazz Air | 47,871 | 0.3% |
| USA 3000 | <u>26,144</u> | <u>0.2%</u> |
| | 2,003,441 | 13.0% |
| Charter | <u>1,856</u> | <u>0.0%</u> |
| Subtotal - International | 2,005,297 | 13.1% |
| Total Enplaned Passengers | 15,362,743 | 100.0% |

Note: The City's Fiscal Year Ends June 30.

TABLE 3

Philadelphia International Airport
Airline Market Shares of Landed Weight (in 1,000 lb. Units)
Fiscal Year 2009

| <u>Airlines</u> | <u>Landed Weight</u> | <u>Percent</u> |
|---------------------------------|----------------------|----------------|
| Domestic | | |
| Scheduled Major / National | | |
| US Airways | 5,522,430 | 24.3% |
| Southwest | 2,825,044 | 12.4% |
| United | 728,405 | 3.2% |
| American | 696,871 | 3.1% |
| Delta | 662,037 | 2.9% |
| Northwest | 421,248 | 1.9% |
| AirTran | 420,984 | 1.9% |
| Continental | 259,085 | 1.1% |
| Midwest | 71,723 | 0.3% |
| Frontier | 57,622 | 0.3% |
| USA 3000 | <u>49,485</u> | <u>0.2%</u> |
| | 11,714,934 | 51.5% |
| Scheduled Regional / Commuter | | |
| US Airways Express | | |
| Republic | 1,764,933 | 7.8% |
| Air Wisconsin | 1,664,552 | 7.3% |
| Piedmont | 998,160 | 4.4% |
| PSA | 253,746 | 1.1% |
| Chautauqua | <u>70,924</u> | <u>0.3%</u> |
| | <u>4,752,315</u> | <u>20.9%</u> |
| Other | <u>568,997</u> | <u>2.5%</u> |
| | 5,321,312 | 23.4% |
| Charter | <u>3,365</u> | <u>0.0%</u> |
| Subtotal - Domestic | 17,039,611 | 74.9% |
| International | | |
| Scheduled | | |
| US Airways | 2,478,569 | 10.9% |
| British | 270,512 | 1.2% |
| Lufthansa | 136,488 | 0.6% |
| Air Wisconsin | 133,433 | 0.6% |
| Air France | 114,804 | 0.5% |
| Air Canada and Jazz Air | 86,187 | 0.4% |
| Air Jamaica | 52,156 | 0.2% |
| USA 3000 | <u>29,862</u> | <u>0.1%</u> |
| | 3,302,011 | 14.5% |
| Charter | <u>5,413</u> | <u>0.0%</u> |
| Subtotal - International | 3,307,424 | 14.5% |
| All-Cargo Airlines | 2,387,809 | 10.5% |
| Total Landed Weight | 22,734,844 | 100.0% |

Note: The City's Fiscal Year Ends June 30.

TABLE 4

**SUMMARY OF HISTORICAL PROJECT REVENUES AND EXPENSES
OF THE AIRPORT SYSTEM
CITY OF PHILADELPHIA
(Fiscal Years Ending June 30)
(Dollar Amounts are listed in thousands)**

| <u>LINE</u> | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|--|-------------|-----------------|-----------------|-----------------|-----------------|
| <u>AMOUNTS AVAILABLE FOR DEBT SERVICE</u> | | | | | |
| 1. Revenue deferred from prior year | \$18,688 | \$22,876 | \$9,621 | (\$12,485) | \$3,304 |
| 1a. Deferred revenue adjustment | | (3,714) | 0 | 6,667 | 0 |
| 2. Space rentals | 44,883 | 47,947 | 55,929 | 75,420 | 83,608 |
| 3. Landing fees | 36,314 | 29,622 | 25,845 | 44,597 | 49,082 |
| 4. Ramp Area rentals | 1,482 | 1,128 | 285 | 800 | 670 |
| 5. Terminal Payments-in-Aid | 13,884 | 9,719 | 0 | 0 | 0 |
| 6. Outside Terminal Area Payments-in-Aid | 982 | 0 | 0 | 0 | 0 |
| 7. International Terminal revenues | 19,553 | 16,919 | 15,370 | 17,722 | 19,673 |
| 8. Revenue (deferred to subsequent year) / accrued for current year | (22,876) | (9,621) | 12,485 | (3,304) | (7,203) |
| 9. Subtotal, Airline Rentals, Fees and Charges | 112,910 | 114,876 | 119,535 | 129,418 | 149,134 |
| 10. Nonairline Revenues | 71,599 | 84,187 | 90,105 | 119,533 | 104,698 |
| 11. Interest income | 618 | 1,724 | 1,619 | 1,594 | 1,420 |
| 12. Total Project Revenues | 185,127 | 200,787 | 211,259 | 250,544 | 255,252 |
| 13. Passenger Facility Charges (PFCs) Available for Debt Service | 32,908 | 32,592 | 32,921 | 32,926 | 32,926 |
| 14. Portion of Fund Balance Attributable to Amounts Available for Debt Service | 0 | 0 | 10,241 | 42,583 | 61,413 |
| 15. Total Amounts Available for Debt Service | 218,035 | 233,379 | 254,421 | 326,053 | 349,590 |
| <u>EXPENSES</u> | | | | | |
| 16. Net Operating Expenses | 71,348 | 77,152 | 87,073 | 99,820 | 99,520 |
| 17. Required Renewal Fund Deposit | 0 | 0 | 0 | 0 | 0 |
| 18. Revenue Bond Debt Service | 88,081 | 88,126 | 85,565 | 84,388 | 95,645 |
| 19. General Obligation Bond Debt Service | 1,051 | 0 | 0 | 0 | 0 |
| 20. Interdepartmental Charges | 57,555 | 57,860 | 70,670 | 89,136 | 89,002 |
| 21. Total Expenses | 218,035 | 223,138 | 243,308 | 273,344 | 284,168 |
| 22. <u>NET REVENUE</u> | \$0 | \$10,241 | \$11,113 | \$52,709 | \$65,422 |
| <u>RATE COVENANT TESTS OF THE ORIGINAL GENERAL ORDINANCE</u> | | | | | |
| 23. Test A (Line 15- Line 16- Line 17) / (Line 18) | 1.67 | 1.77 | 1.96 | 2.68 | 2.61 |
| 24. Test B (Line 15- Line 16- Line 17- Line 20) / (Line 18 + Line 19) | 1.00 | 1.12 | 1.13 | 1.62 | 1.68 |

Note: The information presented above reconciles to the Basic Financial Statements contained in the City's Comprehensive Annual Financial Reports, which are audited by the Office of the City Controller

TABLE 5

**Philadelphia International Airport
History of Applications to Use PFC Revenues
Thru 12/31/2009**

| <u>PFC Application No.</u> | <u>Approval Date</u> | <u>Initial Approved Amount</u> | <u>Amended Approved Amount</u> |
|---------------------------------------|---------------------------------|---|---|
| 93-02-U-00-PHL | 05/15/1993 | 14,250,000 | 12,805,493 |
| 95-03-C-00-PHL | 02/27/1995 | 101,500,000 | 94,683,960 |
| 95-04-U-00-PHL | 10/13/1995 | 950,000 | 1,270,605 |
| 95-05-C-00-PHL | 11/21/1995 | 14,000,000 | 14,000,000 |
| 98-06-C-00-PHL | 02/11/1998 | 26,150,000 | 19,534,950 |
| 99-08-U-00-PHL | 10/12/1999 | 672,000,000 | 999,267,790 |
| 01-09-C-00-PHL | 02/22/2000 | 22,250,000 | 24,400,000 |
| 06-10-C-00-PHL | 02/16/2006 | <u>83,250,000</u> | <u>238,950,000</u> |
| Totals | | 934,350,000 | 1,404,912,798 |

TABLE 6

**Philadelphia International Airport
PFC Revenues Through 12/31/2009**

| <u>FY</u> | <u>COLLECTIONS</u> | <u>INTEREST</u> | <u>TOTAL REVENUES</u> |
|------------------------------|--------------------|-----------------|-----------------------|
| 1993 | 14,484,101 | 142,790 | 14,626,891 |
| 1994 | 22,605,318 | 1,111,511 | 23,716,829 |
| 1995 | 21,828,173 | 2,285,485 | 24,113,658 |
| 1996 | 22,817,704 | 2,277,935 | 25,095,639 |
| 1997 | 27,229,901 | 1,837,334 | 29,067,235 |
| 1998 | 30,931,674 | 1,654,752 | 32,586,426 |
| 1999 | 29,408,652 | 2,018,264 | 31,426,916 |
| 2000 | 32,278,858 | 2,828,083 | 35,106,941 |
| 2001 | 31,880,729 | 3,362,695 | 35,243,424 |
| 2002 | 53,688,877 | 2,112,347 | 55,801,223 |
| 2003 | 43,961,971 | 1,537,729 | 45,499,700 |
| 2004 | 51,766,443 | 808,417 | 52,574,859 |
| 2005 | 61,378,549 | 1,284,025 | 62,662,574 |
| 2006 | 62,165,176 | 3,252,682 | 65,417,858 |
| 2007 | 65,328,768 | 5,047,045 | 70,375,813 |
| 2008 | 70,120,974 | 5,098,760 | 75,219,734 |
| 2009 | 60,898,941 | 1,886,741 | 62,785,682 |
| First 6 Months 2010 | <u>30,491,147</u> | <u>191,992</u> | <u>30,683,139</u> |
| Totals | 733,265,956 | 38,738,586 | 772,004,542 |
| Expenditures thru 12/31/2009 | | | <u>700,764,656</u> |
| Balance | | | <u>71,239,886</u> |

Note: The City's Fiscal Year Ends June 30.

TABLE 7

**Philadelphia International Airport
Historical Enplaned Passengers**

| FY | Domestic | International | Total | Total annual increase (decrease) |
|----------------|--|----------------------|--------------|---|
| 1990 | 7,400,854 | 379,667 | 7,780,521 | |
| 1991 | 7,322,959 | 388,954 | 7,711,913 | -0.9% |
| 1992 | 7,041,274 | 534,004 | 7,575,278 | -1.8% |
| 1993 | 7,645,396 | 582,621 | 8,228,017 | 8.6% |
| 1994 | 7,777,184 | 607,718 | 8,384,902 | 1.9% |
| 1995 | 8,419,133 | 634,955 | 9,054,088 | 8.0% |
| 1996 | 8,538,732 | 665,334 | 9,204,066 | 1.7% |
| 1997 | 9,502,168 | 890,094 | 10,392,262 | 12.9% |
| 1998 | 10,601,187 | 1,104,443 | 11,705,630 | 12.6% |
| 1999 | 10,737,979 | 1,329,813 | 12,067,792 | 3.1% |
| 2000 | 10,652,391 | 1,326,524 | 11,978,915 | -0.7% |
| 2001 | 11,149,732 | 1,521,721 | 12,671,453 | 5.8% |
| 2002 | 10,501,846 | 1,499,659 | 12,001,505 | -5.3% |
| 2003 | 10,519,234 | 1,617,391 | 12,136,625 | 1.1% |
| 2004 | 11,149,952 | 1,938,821 | 13,088,773 | 7.8% |
| 2005 | 13,427,191 | 2,063,378 | 15,490,569 | 18.4% |
| 2006 | 13,563,540 | 2,011,457 | 15,574,997 | 0.5% |
| 2007 | 13,864,721 | 1,987,072 | 15,851,793 | 1.8% |
| 2008 | 13,971,056 | 2,081,917 | 16,052,973 | 1.3% |
| 2009 | 13,357,446 | 2,005,297 | 15,362,743 | -4.3% |
| First 6 months | | | | |
| 2009 | 6,964,869 | 976,456 | 7,941,325 | -2.6% |
| 2010 | 6,796,292 | 1,058,292 | 7,854,584 | -1.1% |
| | Average annual percent increase | | | |
| 1990-2001 | 3.8% | 13.5% | 4.5% | |
| 1996-2001 | 5.5% | 18.0% | 6.6% | |
| 2001-2009 | 2.3% | 3.5% | 3.4% | |

Note: The City's Fiscal Year ends June 30.

FINANCIAL STATEMENTS OF THE DIVISION OF AVIATION

For purposes of calculating Scheduled Airline rentals, fees and charges, and demonstrating compliance with the Rate Covenant, Aviation Fund accounts are maintained on the accrual basis of accounting adjusted to meet the particular requirements of the General Airport Revenue Bond Ordinance of the City. Using this basis of accounting, revenues are recorded as they are earned, and operating expenses are recorded as they are incurred. In addition, principal payments on debt are recorded as an element of expense in lieu of depreciation, and equipment purchases and other capital outlays funded from operations are charged to expense in the year of acquisition.

For purposes of budgeting, Aviation Fund accounts are maintained on the modified accrual basis of accounting also referred to as the “legally enacted basis.” Under this basis, revenues are recorded in the year received. Obligations are recognized and recorded as expenses at the time they are paid or encumbered. A reserve is maintained for encumbrances at the close of the fiscal year, intended to be sufficient to liquidate the estimated related obligations.

The accounting policies of the City of Philadelphia, as reflected in the accompanying Aviation Fund financial statements, conform to accounting principles generally accepted in the United States of America for local government units as prescribed by the Governmental Accounting Standards Board. Accounting principles generally accepted in the United States of America for proprietary funds, such as the Aviation Fund, require that both earnings and expenses be recorded as they accrue, and that depreciation of fixed assets be recorded as an expense. The financial statements for fiscal year 2009 are presented in accordance with accounting principles generally accepted in the United States of America.

The financial statements contained in Appendix I are reconcilable with the Basic Financial Statements contained in the City’s Comprehensive Annual Financial Report for fiscal year 2009, which are audited by the Office of the Controller of the City of Philadelphia.

CITY OF PHILADELPHIA
AVIATION FUND
Appendix I

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CITY OF PHILADELPHIA
AVIATION FUND
Management's Discussion and Analysis
June 30, 2009

INTRODUCTION

The following discussion and analysis of the financial performance and activity of the City of Philadelphia Airport System (the Airport System) is to provide an introduction and understanding of the basic financial statements of the Philadelphia Aviation Fund (Aviation Fund) for the fiscal year ended June 30, 2009 (Fiscal 2009) with selected comparative information for the fiscal year ended June 30, 2008 (Fiscal 2008). Philadelphia International Airport (PHL, or the Airport) and Northeast Philadelphia Airport (PNE) comprise the Airport System, which is owned by the City of Philadelphia (the City) and operated by the Division of Aviation (the Division).

This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes thereto that follow this section. The financial statements presented are for the Aviation Fund only, and are not intended to present fairly the financial position of the City as a whole and the results of its operations and cash flows. The Comprehensive Annual Financial Report (CAFR) of the City provides complete financial information as to the City and its component units.

AIRPORT ACTIVITIES AND HIGHLIGHTS

- ➔ **Financial Position:** The Airport continued to strengthen its financial position in Fiscal 2009, as revenues exceeded expenses by \$38.5 million, and assets exceeded liabilities by \$798 million, a 5.1% increase from last year. This amount includes Aviation Fund unrestricted net assets of \$77.7 million to supplement continuing operations.
- ➔ **Passenger Traffic:** In Fiscal 2009, PHL saw its first reduction in passenger traffic since the events of September 11, 2001. The 4.3% reduction in enplanements resulted primarily from the decline in the global economy, causing airlines to reduce flights and cut seat capacity to enhance economies and efficiencies. PHL's passenger reduction was less severe than the national average of 7.9% for the period, as reported by the Bureau of Transportation Statistics. Aircraft operations and landed weight incurred similar reductions with decreases of 4.1% and 4.6% respectively.

| Enplanements and Operations Activity at PHL | | | |
|--|------------------------|------------------------|--|
| | Fiscal 2009 | Fiscal 2008 | % Increase (Decrease) from 2008 |
| Enplanements (Outbound passengers): | 15,362,743 | 16,052,973 | -4.3% |
| Operations (Takeoffs & landings): | 478,573 | 499,281 | -4.1% |
| Landed Weight (1,000-pound units): | 22,734,844 | 23,823,664 | -4.6% |

CITY OF PHILADELPHIA
AVIATION FUND

Management's Discussion and Analysis
June 30, 2009

- ➔ **Airport Revenue Bonds:** In December 2008, the City remarketed its Series 2005C variable rate bonds (\$178.6 million), with enhancement provided by an irrevocable direct pay letter of credit from TD Bank. This remarketing was undertaken to improve the weekly pricing of the 2005C bonds, which had been unfavorably affected by financial market turmoil and bond insurer downgrades. Since remarketing the bonds, pricing has returned to satisfactory levels, with interest costs running an average \$400,000 per month lower than those incurred prior to the remarketing.

In April 2009, the City issued its fixed rate Series 2009A Airport Revenue Bonds totaling \$45.7 million to refund the Series 2005B variable rate bonds. The 2009A bonds were marketed to take full advantage of the two-year Alternative Minimum Tax (AMT) exemption for airport bonds, instituted under the American Recovery and Reinvestment Act (ARRA). By refunding the 2005B AMT bonds with 2009A non-AMT bonds, the Airport achieved a present value savings of \$5.7 million.

- ➔ **International Air Service:** During 2009, US Airways instituted PHL nonstop service to Birmingham, England, Oslo, Norway and Tel-Aviv, Israel. In October 2009, US Airways announced a system-wide operational realignment that included suspension of service to four low-performing routes: Birmingham, England, Milan, Italy, Shannon, Ireland and Stockholm, Sweden. These four destinations constituted less than 4% of PHL's total international passenger traffic. US Airways presently operates 22 daily flights to 17 cities in 13 countries throughout Europe, serves one Middle East destination and 15 Caribbean and Latin American destinations.
- ➔ **Grant Funding:** In April 2009, the U.S. Department of Transportation awarded PHL \$5 million in ARRA funds. These funds along with FAA Airport Improvement Program (AIP) grants totaling \$8.8 million, will be used to rehabilitate Runway 9R/27L, PHL's longest and widest runway. In June 2009, the Department of Homeland Security (DHS) awarded PHL \$26.6 million in ARRA funds for the construction of Terminal A East in-line baggage systems and related improvements. In October 2009, DHS awarded PHL approximately \$4.9 million in funds for the acquisition and installation of new closed circuit television cameras (CCTV), recording equipment and upgrades to existing componentry. The above DHS grants are designed to expand baggage screening capabilities, enhance baggage throughput and enhance airport security.
- ➔ **Terminal D-E Renovation and Expansion Project:** The first major phase of this \$300 million project, the Terminal D/E Connector, opened in December 2008 featuring a new 14-lane security checkpoint equipped with advanced screening technology and ten new food and retail shops. In February 2010, the Airport completed the second major phase of the project with the expansion of Concourse E, which added seven gates, a 500-seat holdroom area, restrooms, a food court, and permanent artwork from an internationally renowned artist. The next phase to be completed in the spring of 2010 will include a new 9,000 square foot D/E baggage claim connector with two new baggage carousels. The final phase, scheduled for completion by the end of 2010, includes the construction of an expanded ticketing lobby with twenty additional ticket counter positions and an additional 50,000 square foot baggage makeup area with eight inline explosive detection machines.

CITY OF PHILADELPHIA
AVIATION FUND
Management's Discussion and Analysis
June 30, 2009

➔ **Parking**

- **Economy Parking:** To expand its public parking facilities, the Airport's former overseas terminal was demolished, and the site was transformed into an 800-parking space addition to PHL's economy lot, which included the addition of a five-lane toll plaza as a new entrance to the lot. The Philadelphia Parking Authority (PPA) operates five garages, a short-term parking area and, a remote economy lot for the Airport. These facilities total 18,100 parking spaces.
 - **Technology Upgrade:** In the fall of 2009, the PPA completed a \$5.5 million technology project in its garages, which provided License Plate Recognition capability, credit card in/out access and a parking guidance system.
 - **New Cell Phone Lot:** In December 2009, the Airport opened a 150-vehicle on-airport cell phone lot. The lot is free of charge, located within the former footprint of State Route 291 and is easily accessible to drivers arriving at the Airport from all directions. Project costs totaled approximately \$500,000.
- ➔ **Extension of Runway 17-35:** The extension of Runway 17-35 was completed in December 2008 and commissioned by Federal Aviation Administration (FAA) on February 12, 2009. The extension added 1,040-feet to the north/south runway, increasing it from 5,460 feet to 6,500 feet and enabling it to handle narrow-body and regional jets, which account for 75% of aircraft operations at PHL. This project has increased airfield capacity, reduced flight delays by approximately 8%, is projected to save the airlines \$20 million a year in aircraft direct operating costs and generate a net savings in passenger time, valued at \$29 million annually. The project includes new airfield lighting, extension of adjacent taxiways and substantial modifications to nearby roadways and parking facilities. Project costs totaled \$70 million.
- ➔ **Capacity Enhancement Program:** In September 2008, the FAA issued a Draft Environmental Impact Statement (DEIS) for the Airport's Capacity Enhancement Program. The DEIS assessed the potential environmental impacts associated with various concept designs to ease congestion, minimize delays and increase airfield capacity to accommodate demand beyond the year 2020. After issuing the DEIS, the FAA conducted a series of public hearings within the Airport region. FAA expects to issue the final EIS in the summer of 2010 and a Record of Decision by the end of calendar year 2010.
- ➔ **Environmental Stewardship:** PHL has been a grant recipient of FAA's Voluntary Airport Low Emissions (VALE) program since 2005. To date, VALE funding has subsidized 75% of the differential cost of three hybrid vehicles and 75% of the total cost for 20 electrical re-chargers for airline ground service equipment. PHL received approximately \$4 million VALE funding during Fiscal 2008 and an additional \$10.4 million in Fiscal 2009. The 2009 grants will fund the purchase and installation of 25 electric re-charger stations and 24 Pre-Conditioned Air Units and is expected to be completed in the fall of 2010.

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➔ **Awards and Recognition**

- **Philadelphia Marketplace:** Continuing Philadelphia Marketplace's long tradition of excellence in Airport concessions, several of Marketplace's Airport merchants garnered special recognition in the "Best Airport & Concessions Awards" at the 2009 Airport Revenue Conference and Exhibition.

- **American Red Cross:** The Southeastern Pennsylvania Chapter of the American Red Cross named the Airport a recipient of the Authorized Provider Award at the organization's recent "Help Can't Wait Awards" ceremony. The Red Cross recognized the Airport for its ongoing efforts in certifying employees as CPR/AED trainers (cardio pulmonary resuscitation and automated external defibrillation), and its ongoing commitment to these programs.

DESCRIPTION OF PHILADELPHIA AIRPORT SYSTEM

PHL is classified by the Federal Aviation Administration as a large air traffic hub (enplaning 1.0% or more of the total passengers enplaned in the U.S.). According to data reported by Airports Council International – North America, PHL was ranked as the eighteenth busiest airport in the United States, serving 32.3 million passengers in 2008, and is presently the eleventh busiest in the world, and ninth in the nation, based on aircraft operations.

The Airport serves residents and visitors from a broad geographic area that includes eleven counties within four states: Pennsylvania, New Jersey, Delaware and Maryland. The Airport System consists of the following:

Philadelphia International Airport

- **Land.** Approximately 2,328 acres located partly in the southwestern section of the City and partly in the northeastern section of Delaware County, about 7.2 miles from center city Philadelphia.
- **Runways.** The Airport's runway system consists of parallel runways 9L-27R and 9R-27L, crosswind runway 17-35, commuter runway 8-26, and interconnecting taxiways.
- **Terminal Building.** Approximately 2.9 million square feet, consisting of seven terminal units (A West, A East, B, C, D, E and F). Terminal facilities principally include: ticketing areas, passenger holdrooms, baggage claim and approximately 160 food, retail and service establishments.
- **Cargo Facilities.** Located in seven major structures in and around Cargo City at the western end of the Airport.
- **Outside Terminal Area.** Consisting of a 14-story, 400-room hotel, six rental car facilities and five parking garages and surface lots operated by the Philadelphia Parking Authority.

Northeast Philadelphia Airport

PNE is located on 1,150 acres situated within the City limits, 10 miles northeast of center city Philadelphia. PNE serves as a reliever airport for PHL and provides for general aviation, air taxi, corporate, and occasional military use. The airport currently has no scheduled commercial service.

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There are presently eighty-five (85) T-hangars, nine (9) corporate hangars and six open hangars for general aviation activities. There are approximately 210 general aviation based aircraft at PNE.

BACKGROUND INFORMATION ON THE AVIATION FUND

The Aviation Fund is an enterprise fund of the City. Enterprise funds are established by governmental units to account for services that are provided to the general public on a user charge basis and are operated in a manner similar to business-type activities. The Aviation Fund was created and authorized as part of the Fiscal 1974 Operating Budget Ordinance approved by City Council on June 7, 1973 and made effective July 1, 1973.

The Aviation Fund is self-supporting, using aircraft landing fees, terminal building rentals, concession revenue and other facility charges to fund annual expenses. The Airport's capital program is funded by airport revenue bonds issued by the City, federal and state grants, Passenger Facility Charges (PFCs) and operating revenues.

FINANCIAL STATEMENTS OVERVIEW

The basic financial statements of the Aviation Fund are designed to provide readers with a broad overview of Airport System finances, in a manner similar to the private sector. The financial statements are prepared in accordance with generally accepted accounting principles promulgated by the Government Accounting Standards Board (GASB).

Financial statements of the Aviation Fund are presented on an accrual basis, and accordingly, income is recorded as earned and expenses as incurred. Operating revenues include charges for goods and services, rentals and concessions. Operating expenses include the purchase of services, payroll and employee benefits, materials and supplies and depreciation/amortization. Non-operating revenue and expense items include interest income, interest expense, PFC revenues and operating grants.

Aviation Fund financial activity is presented in three financial statements:

- The *Statement of Net Assets* presents information on all Aviation Fund assets and liabilities, classified between current and non-current. The difference between assets and liabilities is reported as *net assets*. Net assets is segregated into four components: invested in capital assets, net of related debt; restricted for capital projects; restricted for debt service; and unrestricted net assets.
- The *Statement of Revenues, Expenses and Changes in Fund Net Assets* presents revenue and expense activity for the current year. The difference between revenue and expense will either increase or decrease total net assets. The ending balance of net assets resulting from this increase or decrease is reflected on the Statement of Net Assets.
- The *Statement of Cash Flows* presents the actual inflow and outflow of cash by category during the year. The difference between the inflow and outflow of cash increases or decreases the total cash balance. The resulting ending cash balance is reflected on the Statement of Net Assets.

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The Aviation Fund financial statements can be found on pages 15 through 17 of this report.

Notes to Financial Statements. The Notes provide additional information that is essential to a full understanding of the data provided in the Aviation Fund financial statements. The Notes to Financial Statements can be found on pages 18 through 42 of this report.

Other information. In addition to the basic financial statements and accompanying notes, government accounting standards require presentation of *required supplementary information (RSI)* concerning the progress in funding employee pension benefit obligations. Discrete pension information is not available for the Aviation Fund, but is available for the City as a whole. Please see the Comprehensive Annual Financial Report (CAFR) of the City of Philadelphia for complete financial information for the City and its component units.

FINANCIAL POSITION

The following table summarizes the Airport System's assets, liabilities and net assets at June 30, 2009 and June 30, 2008:

City of Philadelphia – Aviation Fund
Statement of Net Assets
(amounts expressed in thousands)

| | 2009 | 2008 | Increase (Decrease) from 2008 | % Increase (Decrease) from 2008 |
|--|------------|------------|-------------------------------------|---------------------------------------|
| Current and other assets | \$ 558,569 | \$ 655,063 | \$ (96,495) | -14.7% |
| Capital assets | 1,596,402 | 1,474,348 | 122,054 | 8.3% |
| Total assets | 2,154,971 | 2,129,411 | 25,560 | 1.2% |
| Long-term liabilities | 1,225,705 | 1,255,346 | \$ (29,640) | -2.4% |
| Other liabilities | 131,454 | 114,727 | 16,727 | 14.6% |
| Total liabilities | 1,357,160 | 1,370,073 | (12,913) | -0.9% |
| Net assets: | | | | |
| Invested in capital assets, net of related debt | 560,028 | 479,583 | 80,445 | 16.8% |
| Restricted for Capital Projects | 52,445 | 81,674 | (29,229) | -35.8% |
| Restricted for Debt Service | 107,607 | 112,613 | (5,006) | -4.4% |
| Unrestricted | 77,731 | 85,468 | (7,737) | -9.1% |
| Total net assets | \$ 797,811 | \$ 759,338 | \$ 38,473 | 5.1% |

Net Assets serves as a useful indicator of the Airport's financial position and is a measurement of the financial condition of the Airport at a specific point in time. At June 30, 2009, the Airport System's assets exceeded liabilities by \$798 million. Between Fiscal 2008 and Fiscal 2009, total net assets increased by \$38 million. Changes in total net assets are summarized below:

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- **Total Assets** increased \$25.6 million. Capital assets increased by \$122.1 million due to capital asset additions, resulting from ongoing Airport expansion projects, exceeding depreciation. This overall increase was offset by a decrease of \$96.5 million in current and other assets due primarily to construction payments exceeding receipts for PFC's, grants and investment earnings.
- **Total Liabilities** decreased \$12.9 million as a result of long-term liability decreases caused by the repayment of debt. These decreases were offset by the increases in current liabilities, mainly for construction accounts payable.
- **Invested in capital assets, net of related debt** increased by \$80 million due to an increase in capital construction of \$194 million, which was offset by \$72 million in accumulated depreciation. This net increase in capital assets of \$122 million was offset by an increase in related debt of \$42 million. Although these capital assets assist the Airport in providing services to the traveling public, they are generally not available to fund operations of future periods.
- **Restricted for capital projects** represents funds available and restricted for construction of capital assets, reduced by debt payable on those funds. This balance decreased by \$29 million in Fiscal 2009 because PFC expenditures exceeded PFC revenues by \$29 million.
- **Restricted for debt service** decreased \$5 million due to changes in Sinking Fund and Sinking Fund Reserve requirements as a result of the restructuring and refunding of certain bond issues.
- **Unrestricted net assets** decreased by \$8 million. Unrestricted net assets may be used to supplement the Airport System's ongoing operations.

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The following table compares the changes in revenues, expenses and fund net assets between Fiscal 2009 and Fiscal 2008:

City of Philadelphia – Aviation Fund
Statement of Revenues, Expenses and Changes in Fund Net Assets
(amounts expressed in thousands)

| | 2009 | 2008 | Increase (Decrease) from 2008 | % Increase (Decrease) from 2008 |
|---------------------------------------|-------------------|-------------------|--|--|
| Revenues: | | | | |
| Operating income | \$ 251,703 | \$ 238,357 | \$ 13,346 | 5.6% |
| Operating grants and contributions | 2,052 | 1,917 | 135 | 7.1% |
| Capital grants and contributions | 44,744 | 33,603 | 11,142 | 33.2% |
| Passenger facility charges | 61,255 | 64,855 | (3,600) | -5.6% |
| Interest income | 1,568 | 20,687 | (19,119) | -92.4% |
| Total revenues | <u>361,323</u> | <u>359,419</u> | <u>1,904</u> | <u>0.5%</u> |
| Expenses: | | | | |
| Operating expenses | 270,407 | 260,006 | 10,401 | 4.0% |
| Debt service interest | 52,086 | 57,669 | (5,583) | -9.7% |
| Other expenses | 357 | 5,441 | (5,084) | -93.4% |
| Total expenses | <u>322,850</u> | <u>323,116</u> | <u>(266)</u> | <u>-0.1%</u> |
| Increase in Net Assets | <u>38,473</u> | <u>36,303</u> | <u>2,170</u> | <u>6.0%</u> |
| Net assets beginning of year | 759,338 | 722,572 | 36,767 | 5.1% |
| Prior Period Adjustment | - | 464 | (464) | -100.0% |
| Net assets adjusted beginning of year | <u>759,338</u> | <u>723,035</u> | <u>\$ 36,303</u> | <u>5.0%</u> |
| Net assets end of year | <u>\$ 797,811</u> | <u>\$ 759,338</u> | <u>\$ 38,473</u> | <u>5.1%</u> |

Changes in net assets represent the results of operations and are useful indicators of whether the overall financial condition of the Airport has improved or declined during the year. In Fiscal 2009, net assets increased \$38 million, or 5.1%, from the prior year. This increase reflects Airport net income and capital contributions. Airport income before capital contributions is composed of operating and non-operating revenues, net of expense. Capital contributions represent federal and state grants for approved capital projects.

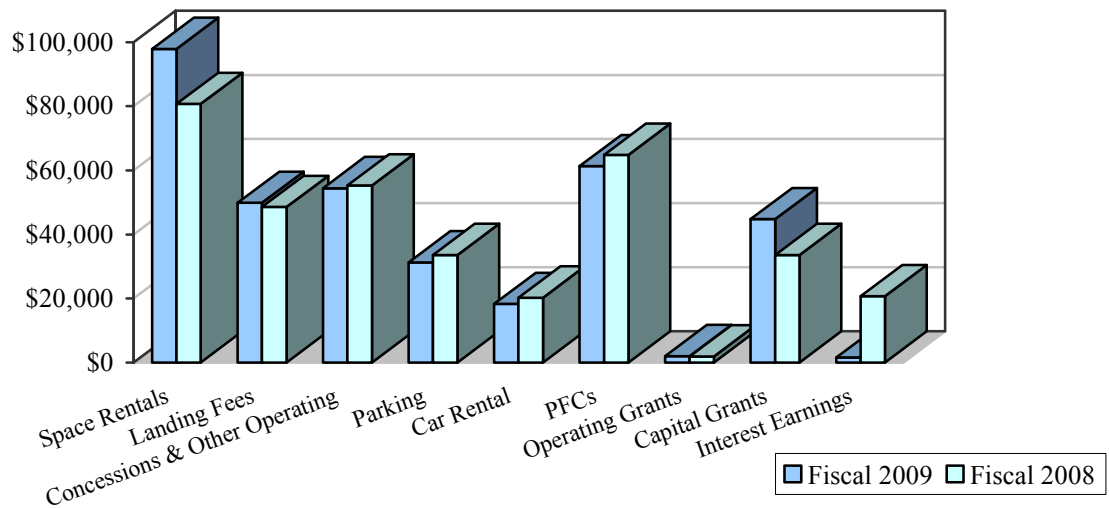
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Revenues

Approximately 71% of all revenue came from operating sources, which include space rentals, landing fees and revenues from parking, concessions and car rentals. PFCs account for another 17%, with the remainder coming from Federal and State grants, and interest earnings.

The graph below presents the major components of revenue for Fiscal 2009 and 2008, followed by explanations of significant changes in these categories between years.

Revenues by Source (Thousands)



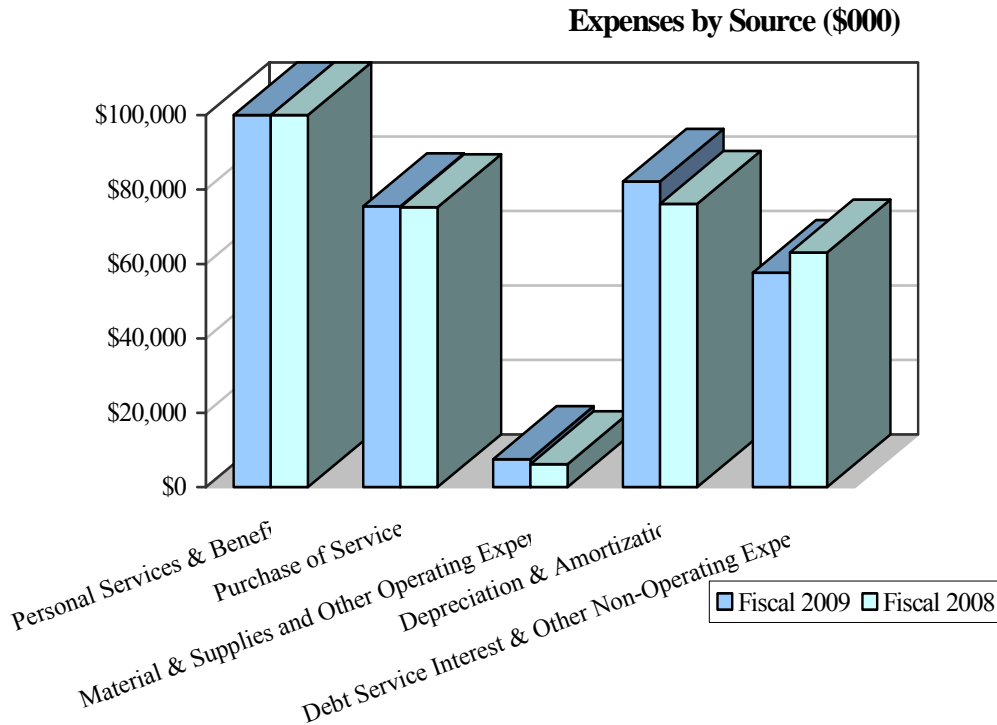
- ➔ Operating revenues, which include the first five categories in the bar graph above, increased approximately 6% in Fiscal 2009. Terminal rental and signatory landing fee revenues increased 12% and 20%, respectively, in fiscal 2009, but were offset by decreases in concessions, parking and car rental revenues as a result of the decrease in passenger traffic.
- ➔ PFC revenue decreased approximately 6% due primarily to a reduction in enplaned passengers in Fiscal 2009.
- ➔ Capital grants increased in Fiscal 2009 as a result of a new grant agreement for the TSA Explosives Detection System (EDS) project. The TSA EDS agreement applies retroactively to selected expenditures from Fiscal 2007 forward. The amount of revenue earned for the TSA EDS grant for 2009 was \$12 million. Other Fiscal 2009 grant revenue remained stable relative to Fiscal 2008. It should be noted that capital grant revenue in any given year is dependent upon construction timelines for grant eligible Airport capital projects.
- ➔ Interest earnings decreased because of reduced market interest rates. Also, \$8.6 million of interest income was used to offset interest expense capitalized to construction in progress during 2009.

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Expenses

Airport expenses result from a wide range of services; wages, benefits and contractual services account for approximately 55% of total expenses. Depreciation and amortization comprise roughly 25% of the total, and the remainder consists of debt service interest and other operating and non-operating expenses.

The graph below presents the major components of expense for Fiscal 2009, followed by explanations of significant changes in these components from Fiscal 2008.



- ➔ Personal services and benefits increased slightly in Fiscal 2009 primarily due to increased amounts in workers compensation liability and compensated absences, which were offset by cost containment measures that were instituted through hiring and wage freezes, and additional overtime controls.
- ➔ Purchase of services did not change significantly from Fiscal 2008 to Fiscal 2009 due to self-imposed budget reductions by the Division.
- ➔ Material and supplies and other operating expenses increased slightly due to additional purchases made during Fiscal 2009.
- ➔ Depreciation and amortization increased almost 8% in Fiscal 2009 due to construction of new capital assets. The straight-line method is used to record depreciation.
- ➔ Debt service interest and other non-operating expenses decreased approximately 17% in Fiscal 2009 due to capitalization of interest on the significant construction in progress during the year.

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CAPITAL ASSET AND DEBT ADMINISTRATION

The Airport's investment in capital assets, net of accumulated depreciation, amounted to \$1.6 billion at the end of the current fiscal year. The following table presents the changes in capital assets for Fiscal 2009.

City of Philadelphia – Aviation Fund
Capital Assets
(amounts expressed in thousands)

| | July 1, 2008 | Additions | Deletions | June 30, 2009 |
|---|--------------|------------|--------------|---------------|
| <u>Non-Depreciable Business Type Assets</u> | | | | |
| Land | \$ 88,433 | \$ - | \$ - | \$ 88,433 |
| Construction in Progress | 76,246 | 198,258 | (126,287) | 148,217 |
| Total Non-Depreciable Business Type Assets | 164,679 | 198,258 | (126,287) | 236,650 |
| <u>Depreciable Business Type Assets</u> | | | | |
| Buildings | 1,719,021 | 96,866 | (10,094) | 1,805,793 |
| Infrastructure | 523,056 | 34,601 | - | 557,657 |
| Equipment | 44,597 | 2,573 | (2,412) | 44,758 |
| Total Depreciable Business Type Assets | 2,286,674 | 134,040 | (12,506) | 2,408,208 |
| <u>Accumulated Depreciation</u> | | | | |
| Capital Additions | (703,509) | (57,490) | 8,708 | (752,291) |
| Infrastructure | (248,198) | (21,149) | - | (269,348) |
| Equipment | (25,298) | (3,518) | 1,998 | (26,817) |
| Total Accumulated Depreciation | (977,005) | (82,157) | 10,706 | (1,048,456) |
| Net Depreciable Business Type Assets | 1,309,669 | 51,883 | (1,800) | 1,359,752 |
| Total Business Type Assets | \$ 1,474,348 | \$ 250,141 | \$ (128,087) | \$ 1,596,402 |

Capital Assets

Major capital asset events for which capital expenditures were incurred during Fiscal 2009 include the following:

- ➔ *Construction in Progress.* Additions to construction in progress totaled \$198.3 million during Fiscal 2009. Major projects that were under construction during the fiscal year included: expansion and modernization of Terminals D and E; resurfacing of runway 9R/27L; extension of Runway 17-35; improvements to Terminal A East; noise compatibility program; expansion of employee lot; and Terminal A West bag recheck system. Substantially completed projects, identified below, were transferred from construction in progress to capital assets.

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➔ *Buildings, Infrastructure & Equipment.* Fixed asset additions totaled \$134.0 million during Fiscal 2009. Significant design and construction projects substantially completed during Fiscal 2009 include the following:

- Terminal D&E Expansion & Modernization – completed phases (\$60.1 million)
- Runway 17–35 Extension – completed phases (\$30.4 million)
- Terminal A West – Bag Recheck System – completed phases (\$5.1 million)
- Concessions Terminal Expansion (\$3.1 million)
- Facility Management System (\$4.7 million)
- Airport Master Plan/Environmental Impact Statement – completed phases (\$4.2 million)
- Terminal F Renovations & Expansion – completed phases (\$2.5 million)
- Noise Programs (\$2.8 million)

Long-Term Debt

Principal paid on debt instruments totaled \$77 million for Fiscal 2009, which included refunding the Series 2005B bonds in the amount of \$41 million. Interest payments on debt instruments totaled \$72.2 million for Fiscal 2009. The following table summarizes the changes in long-term debt, including the current portion, for Fiscal 2009:

City of Philadelphia – Aviation Fund
Changes in Long-Term Debt
(amounts expressed in thousands)

| | <u>July 1, 2008</u> | <u>Additions</u> | <u>Retirements/ Repayments</u> | <u>June 30, 2009</u> |
|---------------|---------------------|------------------|------------------------------------|----------------------|
| Revenue bonds | \$ 1,302,800 | \$ 45,715 | \$ 77,305 | \$ 1,271,210 |

As of June 30, 2009, total revenue bonds payable, less current maturities of \$38.5 million, equated to \$80.35 per enplaned passenger, compared to \$78.90 as of June 30, 2008.

Due to financial instability within the bond insurance and credit markets that began in 2008, the City has taken certain steps to minimize market-related cost increases and to ensure compliance with the Amended and Restated General Airport Revenue Bond Ordinance of 1995 (the Bond Ordinance):

- In April 2009, the City issued Airport Revenue Refunding Bonds Series 2009A sub series (1) through (3) in the amount of \$45.7 million. Serial bonds were issued in the amount of \$25.7 million with interest rates ranging from 1.5% to 5.0% maturing in 2023.

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Term bonds were issued in the amounts of \$3.9 million and \$16.1 million with interest rates ranging from 5.0% to 5.375% maturing in 2024 and 2029 respectively. The gain/loss on the bonds cannot be calculated in the usual way because the refunded bonds (series 2005B) were variable rate bonds, while the 2009A refunding bonds are fixed rate bonds. The 2005B bonds were subject to the Alternative Minimum Tax ("AMT"). However, the 2009A refunding bonds were issued on a fixed rate, non-AMT basis. The proceeds of the bonds, together with other monies of the City, were used to (1) current refund the City's outstanding Airport Revenue Bonds Series 2005B, (2) fund a deposit to the Parity Sinking Fund Reserve Account in respect of the bonds, and (3) pay the costs of issuance of the bonds.

- In December 2008, the outstanding balance of \$178.6 million of City of Philadelphia Airport Revenue Refunding Bonds Series 2005C was remarketed under an irrevocable direct pay letter of credit (LOC) from TD Bank. The TD Bank LOC replaces a bond insurance policy from MBIA Insurance Corporation and the liquidity facility provided by JP Morgan Chase Bank, N.A. pursuant to standby bond purchase agreement, issued simultaneously with the issuance of the 2005C bonds in June 2005, and the surety policy for the sinking fund reserve account for the 2005C bonds. The LOC constitutes both a Credit Facility and Liquidity Facility under the Airport's General Bond Ordinance and the Variable Rate Securities Agreement, and TD Bank N.A. will be the Credit Provider and Liquidity Provider under the Ordinance and the Variable Rate Securities Agreement for the 2005C bonds. The bonds will have a weekly interest rate and maturing in 2025.

BUDGETARY HIGHLIGHTS FROM FISCAL 2009

Actual expenditures for Fiscal 2009 were 1.8% lower than budgeted expenditures. As economic conditions worsened during the year, the Airport instituted cost containment measures and deferrals to mitigate the impact to the airlines. The results of these initiatives are highlighted below:

- A 9.4% reduction (\$9.3 million) in direct expenses related to Division of Aviation personal services, contractual services, materials and supplies, equipment, and other direct expenses.
- As a partial offset to the above spending reductions, net interdepartmental charges were 3.8% (\$3.4 million) higher than projected due to the following: higher than budgeted fringe benefit rates attributable to increasing costs for health care and pension; increased police costs due to enhanced security measures mandated by the Transportation Security Administration; and increased costs resulting from the purchase of vehicles previously deferred.
- Net debt service was 2.1% (\$1.3 million) greater than budgeted as a result of less than anticipated excess interest income in sinking fund reserves accounts, which is used to pay debt service.

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KEY FACTORS AFFECTING THE FISCAL 2010 OPERATING BUDGET

The Airport System's Fiscal 2010 operating budget increased by 2.4% from Fiscal 2009 due to the following factors:

- A 7.0% increase (\$6.0 million) in net interdepartmental charges due to anticipated increases in the citywide health care and pension costs, and projected wage increases for uniformed employees.
- A \$2.6 million increase (4.3%) in net debt service attributable to the anticipated completion of various capital projects funded by the 2005A and 2007A Bonds. Debt service on these capital projects was previously capitalized.
- The above increases to the Fiscal 2010 budget were offset by the Division instituting budgetary restrictions in response to global economic conditions, which have resulted in lost profits and capacity reductions in the airline industry. These cost containment measures resulted in a decrease to the Division's Fiscal 2010 budget in the following areas: personal services (\$343,000); professional services (\$1.9 million); materials and supplies (\$630,000); legal services (\$136,000); and services to others (\$1.8 million).

The FY 2010 snow removal budget was based on an assumption of average snowfall totals for the winter of 2009/10. In actuality, snow totals and major snow events for the Philadelphia region have reached their highest levels in recorded history. As a result, the Airport expects that its FY 2010 snow removal costs will exceed original projections by approximately \$7 million, equivalent to 2.7% of the Airport's annual budget. To fund the additional snow costs, the Airport has imposed mid-year spending limits and is considering other funding measures, including landing fee rate revisions, a limited use of operating reserves, a potential for federal funding assistance, or a combination thereof.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of Philadelphia Airport System finances and to demonstrate the City's accountability for the funds it receives and disburses. For additional information concerning this report, please contact: Edward C. Anastasi, Deputy Director of Aviation - Finance and Administration, Philadelphia International Airport, Executive offices, Terminal D, 3rd Floor, Philadelphia, PA 19153.

CITY OF PHILADELPHIA

AVIATION FUND

Statement of Net Assets

June 30, 2009

ASSETS

Current assets:

| | |
|-----------------------------------|--------------------|
| Cash and cash equivalents | \$ 102,127,351 |
| Accounts receivable: | 12,173,175 |
| Allowance for doubtful accounts | (1,084,457) |
| Inventories | 2,962,601 |
| Due from other governmental units | 964,732 |
| Total current assets | <u>117,143,402</u> |

Restricted assets:

| | |
|--|--------------------|
| Cash and cash equivalents | 333,790,762 |
| Cash held by fiscal agent | 30,317,551 |
| Sinking funds and reserves held by fiscal agents | 47,154,404 |
| Grants from other governments for capital purposes | 13,529,809 |
| Receivables | 8,533,811 |
| Total restricted assets | <u>433,326,337</u> |

Net pension assets

8,099,111

Property, plant and equipment:

| | |
|---|----------------------|
| Land | 88,432,784 |
| Infrastructure | 557,656,992 |
| Construction in progress | 148,217,022 |
| Buildings and equipment | 1,850,551,020 |
| Less: accumulated depreciation and amortization | (1,048,455,811) |
| Property, plant and equipment, net | <u>1,596,402,007</u> |

 Total assets

2,154,970,857

LIABILITIES

Current liabilities:

| | |
|---|--------------------|
| Vouchers payable | 2,685,345 |
| Accounts payable | 11,061,318 |
| Salaries and wages payable | 3,059,917 |
| Construction contracts payable | 44,398,183 |
| Accrued expenses | 16,349,246 |
| Deferred revenue | 15,390,422 |
| Current maturities of long-term bonded debt | 38,510,000 |
| Total current liabilities | <u>131,454,431</u> |

Long-term liabilities:

| | |
|----------------------------------|----------------------|
| Revenue bonds - principal amount | 1,232,700,000 |
| Unamortized discount and loss | (20,822,136) |
| Other long-term liabilities | 13,827,595 |
| Total long-term liabilities | <u>1,225,705,459</u> |
| Total liabilities | <u>1,357,159,890</u> |

NET ASSETS

| | |
|--|-----------------------|
| Invested in capital assets, net of related debt: | 560,027,919 |
| Restricted: | |
| Capital projects | 52,445,053 |
| Debt service | 107,607,368 |
| Unrestricted | 77,730,627 |
| Total net assets | <u>\$ 797,810,967</u> |

See notes to the financial statements.

CITY OF PHILADELPHIA

AVIATION FUND

Statement of Revenues, Expenses and Changes in Fund Net Assets

For the Year Ended June 30, 2009

Operating revenues:

| | |
|----------------------------------|--------------------|
| Charges for goods and services | \$ 73,950,707 |
| Rentals and concessions | 173,574,129 |
| Miscellaneous operating revenues | 4,178,104 |
| Total operating revenues | <u>251,702,940</u> |

Operating expenses:

| | |
|-------------------------------|--------------------|
| Personal services | 63,732,083 |
| Purchase of services | 75,493,151 |
| Materials and supplies | 6,586,423 |
| Employee benefits | 41,501,356 |
| Indemnities and taxes | 937,733 |
| Depreciation and amortization | 82,156,722 |
| Total operating expenses | <u>270,407,468</u> |

Operating loss (18,704,528)

Nonoperating revenues (expenses):

| | |
|----------------------------|--------------|
| Operating grants | 2,052,401 |
| Passenger facility charges | 61,255,198 |
| Interest income | 1,567,964 |
| Net pension obligation | (3,736,964) |
| Debt service, interest | (52,085,548) |
| Other revenue (expenses) | 3,380,024 |

Total nonoperating revenues (expenses) 12,433,075

Income before capital contributions (6,271,453)

Capital contributions 44,744,177

Change in net assets 38,472,724

Net assets beginning of period 759,338,243

Net assets end of period \$ 797,810,967

See notes to the financial statements.

**CITY OF PHILADELPHIA
AVIATION FUND**

*Statement of Cash Flows
For the Year Ended June 30, 2009*

CASH FLOWS FROM OPERATING ACTIVITIES:

| | |
|---|----------------|
| Receipts from customers | \$ 255,425,183 |
| Receipts from interfund services | 887,631 |
| Payments to suppliers | (78,762,738) |
| Payments to employees | (100,105,584) |
| Internal activity-payments to other funds | (5,380,432) |
| Other receipts (payments) | 312,517 |
| Net cash provided by operating activities | 72,376,577 |

CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES :

| | |
|--|-----------|
| Grant proceed not specifically restricted for capital purposes | 1,933,517 |
|--|-----------|

**CASH FLOWS FROM CAPITAL AND RELATED
FINANCING ACTIVITIES:**

| | |
|---|---------------|
| Proceeds from capital debt | 44,289,740 |
| Capital contributions | 40,040,026 |
| Purchase of capital assets | (178,441,236) |
| Principal paid on capital debt | (77,305,000) |
| Interest paid on capital debt | (71,963,664) |
| Passenger facility charges | 60,898,941 |
| Net cash provided by capital and related financing activities | (182,481,193) |

CASH FLOWS FROM INVESTING ACTIVITIES:

| | |
|--|------------|
| Proceeds from sale and maturities of investments | 119,523 |
| Interest and dividends | 16,848,022 |
| | 16,967,545 |

NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS:

| | |
|---------------------------|----------------|
| | (91,203,554) |
| Balance beginning of year | 557,439,217 |
| Balance end of year | \$ 466,235,663 |

**RECONCILIATION OF OPERATING (LOSS) TO NET CASH
PROVIDED BY OPERATING ACTIVITIES:**

| | |
|---|-----------------|
| Operating (loss) | \$ (18,704,528) |
| Adjustment to reconcile operating (loss) to net cash provided by operating activities: | |
| Depreciation and amortization | 82,156,722 |
| Changes in assets and liabilities: | |
| Receivables, net | 969,170 |
| Inventories | (28,455) |
| Accounts and other payables | 3,168,928 |
| Deferred revenue | 4,814,740 |
| Net cash provided by operating activities | \$ 72,376,577 |

See notes to the financial statements.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Operations

The Aviation Fund is a proprietary fund of the City of Philadelphia (City). It was created and authorized as part of the Fiscal 1974 Operating Budget Ordinance approved by City Council on June 7, 1973 and became effective July 1, 1973. This fund was established to facilitate administrative and financial operations necessary to maintain, improve, repair and operate Philadelphia International Airport and Northeast Philadelphia Airport. The financial statements presented are for the Aviation Fund only, and are not intended to present fairly the financial position of the City of Philadelphia as a whole and the results of its operations and cash flows. The comprehensive annual financial report of the City of Philadelphia provides complete financial information as to the City and its component units.

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting. Under this method, revenues are recognized in the accounting period in which they are earned and expenses are recognized at the time obligations are incurred.

Private sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government wide and the proprietary fund financial statements to the extent that they do not conflict or contradict guidance of the Governmental Accounting Standards Board (GASB). Governments also have the option of following subsequent private sector guidance for their business type activities and enterprise funds. The City has elected not to follow subsequent private sector guidelines.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's ongoing operations. The principal operating revenue of the Aviation Fund is charges for the use of the airport facilities. Operating expenses for proprietary funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

Deposits and Investments

The Aviation Fund's deposits and investments are held in segregated operating and capital accounts and by an outside fiscal agent. Sinking funds and reserves are maintained in segregated investment accounts, to comply with reserve and other requirements of the bond covenants. No Aviation Fund accounts are commingled with other City funds. All highly liquid investments (except for repurchase agreements) with a maturity of three months or less are considered to be cash equivalents. Investments are recorded at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on national or international exchanges are valued at the last reported sales price.

Statutes authorize the City to invest in obligations of the Treasury, agencies, and instruments of the United States, repurchase agreements, collateralized certificates of deposit, bank acceptance or mortgage obligations, certain corporate bonds, and money market funds. Management is not aware of any violations of statutory authority or contractual provisions for investments for the year ended June 30, 2009.

Accounts Receivable

Accounts receivable included in current assets consists of billed and unbilled rentals and fees, which have been earned but not collected as of June 30, 2009. Credit balance receivables have been included in deferred revenue in the statement of net assets. The allowance for doubtful accounts is management's estimate of the amount of accounts receivable, which will be deemed to be uncollectible and is based upon specific identification. Unpaid accounts are referred to the City's law department if deemed uncollectible. Accounts are written off when recommended by the law department.

Inventories

Inventories consist of materials and supplies and are carried at amounts determined on a moving-average cost basis.

Restricted Assets

Restricted assets represent amounts that have been legally restricted by contracts or outside parties and are not available for payment of operating fund expenditures. The following represent restricted assets of the Aviation Fund:

- Funds available for construction, including grants due from other governments for capital purposes.
- Sinking funds and reserves reserved for debt service and construction, pursuant to revenue bond indentures.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

- Passenger facility charges (PFCs) represent fees remitted by airlines based on passenger ticket sales for flights boarding at Philadelphia International Airport. The fees are reserved for funding certain Federal Aviation Administration (FAA) approved capital projects and debt service payments. Collection of PFCs began in the fall of 1992. All unexpended PFC funds, including accumulated interest, are classified as restricted assets.

Capital Assets

Capital assets include property, plant and equipment and infrastructure assets constructed or acquired by purchase with an initial individual cost in excess of \$5,000 and a useful life in excess of three years. Capital assets are recorded at cost.

Construction in progress includes all direct contract costs plus overhead costs. Overhead costs include direct and indirect engineering and architectural costs and interest incurred during the construction period, for projects financed with bond proceeds. Interest is capitalized on proprietary fund assets acquired with tax exempt debt by offsetting interest expense from the date of borrowing through the project completion with the amount of interest income on the invested proceeds over the same period. After construction is completed, interest income and expense on these funds are recorded as non-operating revenue and expense. Construction in progress is transferred to capital assets when 80% of the estimated project costs have been expended. Depreciation commences in the year following the transfer.

Depreciation and amortization are computed using the straight-line method over the following estimated useful lives:

| | |
|-----------------------------------|----------------|
| Buildings | 20 to 50 years |
| Improvements other than buildings | 10 to 25 years |
| Equipment | 5 to 10 years |

Management periodically reviews its long-lived assets for impairment. At present, management does not believe any impairment exists.

Deferred Revenue

Deferred revenue relates primarily to excess billings to signatory airlines and advance payments received from air carriers. Such deferrals are ultimately included in income when earned, usually during the next year.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

Revenues

Operating revenues consist primarily of the following:

- Charges for goods and services – landing fees, international terminal charges, and utility charges.
- Rental and concessions – space rentals, parking revenue, car rental and concession revenues. Income from lease contracts is recorded when earned. Adjustments to revenue resulting from audits of tenants are recorded as determined. Income from the Philadelphia Parking Authority for operation of the airport parking facilities is recorded in rental and concession income at the amount received. The amount recorded is subject to final audit adjustment.

Non-operating revenues consist primarily of the following:

- Operating grants.
- PFCs –revenue from PFCs is reserved for the funding of certain capital expenditures and debt service payments, as approved by the FAA.
- Interest income.

Capital contributions consist of federal and state grant reimbursements for capital expenditures.

Operating Expenses

Operating expenses consist primarily of personnel and administrative services, purchase of services and depreciation and amortization expense.

Amortization of Discount on Bonded Debt and Loss on Retirement of Bonds

Bond premiums and discounts are deferred and amortized over the life of the debt using the effective interest method. Bonds payable are reported net of applicable premium or discount. Bond issuance costs are reported as deferred charges and are reported over the life of the related debt. The loss on retirement of bonds is amortized on the straight-line method over the life of the new debt issued.

Compensated Absences

It is the City's policy to allow employees to accumulate earned but unused vacation benefits. Vacation pay is accrued as earned. Sick leave balances are not accrued in the financial statements because sick leave rights are non-vesting.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

Management's Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. DEPOSITS AND INVESTMENTS

For the year ended June 30, 2009, deposits and investments are included in the financial statements in current and restricted cash and cash equivalents, in sinking funds and reserves held by fiscal agents, and in cash held by fiscal agent.

Deposits

State statutes require banks to collateralize City deposits at amounts equal to or in excess of the City's balance. Such collateral is to be held by the Federal Reserve Bank or the trust department of a commercial bank other than the pledging bank. At year-end, both the carrying amount (book balance) and bank balance of deposits for the Aviation Fund were \$31.8 million. All of the collateralized securities were held in the City's name.

Investments

The City has established a comprehensive investment policy to minimize custodial credit risk for its investments. To minimize custodial risk, the City has selected custodian banks that are members of the Federal Reserve System to hold its investments. Delivery of the applicable investment documents to the City's custodian is required for all investments.

As of June 30, 2009 the fair value of the Aviation Fund's investments consisted of the following:

| | <u>Fair Value</u> | <u>% of Total</u> |
|-----------------------------------|-----------------------|-------------------|
| U.S. Government Securities | \$ 43,341,371 | 8.79% |
| U.S. Government Agency Securities | 299,896,855 | 60.81% |
| Corporate Bonds | 3,721,907 | 0.75% |
| Short-Term Investment Pools | 90,908,506 | 18.43% |
| Repurchase Agreements | 10,658,601 | 2.16% |
| Commercial Paper | 44,676,636 | 9.06% |
| | <u>\$ 493,203,876</u> | <u>100.0%</u> |

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

Interest Rate Risk: The City’s investment portfolio is managed to accomplish preservation of principal, maintain liquidity and maximize the return on the investments. To limit its exposure to fair value losses from rising interest rates the City’s investment policy limits investments to maturities of no longer than two years, except in sinking fund reserve portfolios.

| | <u>Less Than 1</u> <u>Year</u> | <u>1 - 3 Years</u> | <u>More Than 3</u> <u>Years</u> |
|-----------------------------------|-----------------------------------|----------------------|------------------------------------|
| U.S. Government Securities | \$ 37,698,459 | \$ 5,642,912 | \$ - |
| U.S. Government Agency Securities | 234,790,470 | 64,144,385 | 962,000 |
| Corporate Bonds | 502,765 | 3,219,142 | - |
| Short-Term Investment Pools | 90,908,506 | - | - |
| Repurchase Agreements | - | - | 10,658,601 |
| Commercial Paper | 44,676,636 | - | - |
| | <u>\$ 408,576,835</u> | <u>\$ 73,006,439</u> | <u>\$ 11,620,601</u> |

Credit Risk: For the City as a whole, credit risk is limited by investing in US Government securities (7.8%) or US Government Agency obligations (15.29%). The US Government Agency obligations must be rated AAA by Standard & Poor’s (S&P) or Aaa by Moody’s Investor Services (Moody’s). All US Government Securities meet the criteria. The City’s investment in commercial paper (3.43%) must be rated A1 by S&P and/or MIG1 by Moody’s and the senior long-term debt of the issuer must not be rated lower than A by S&P and/or Moody’s. Commercial paper is also limited to 25% of the portfolio. All commercial paper investments meet the criteria. Of the corporate bonds held by the City, 88.0% had an S&P rating of AAA to AA. Cash accounts are swept nightly and idle cash invested in money market funds (short-term investment pools). Short-term investment pools are rated AAAM by S&P and Aaa by Moody’s. The City limits its foreign currency risk by investing in certificates of deposit and bankers acceptances issued or endorsed by non-domestic banks that are denominated in US dollars providing that the banking institution has assets of not less than \$100 million and has a Thompson’s Bank Watch Service “Peer Group Rating” not lower than II. At the end of the fiscal year the City did not have any investments of that nature.

3. CASH HELD BY FISCAL AGENT

Cash held by fiscal agent consists of year-end cash and investment balances related to the net proceeds of Philadelphia Authority for Industrial Development’s (PAID) Airport Revenue Bonds Series 1998A and 2001A. In accordance with GASB Interpretation #2, these bonds are considered by PAID to be conduit debt. Therefore, no asset related to the bond proceeds or liability related to the bonds is shown on PAID’s financial statements. Instead, the proceeds are held by a fiscal agent and disbursed at the City’s direction to pay for related capital improvements at the airport. Both the assets and liabilities related to the PAID bonds are included in the financial statements of the Aviation Fund.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

4. CAPITAL ASSET ACTIVITY

The following schedule reflects the capital asset activity for the Aviation Fund during the year.

| | Beginning Balance | Additions | Transfers/ Retirements | Ending Balance |
|---|-------------------------|-----------------------|---------------------------|-------------------------|
| Non-depreciable Assets | | | | |
| Land | \$ 88,432,784 | \$ - | \$ - | \$ 88,432,784 |
| Construction-in-progress | 76,245,784 | 198,257,853 | (126,286,615) | 148,217,022 |
| Total non-depreciable business type assets | 164,678,568 | 198,257,853 | (126,286,615) | 236,649,806 |
| Depreciable business type assets | | | | |
| Buildings | 1,483,424,284 | 84,517,619 | (10,093,892) | 1,557,848,011 |
| Infrastructure | 523,055,902 | 34,601,090 | - | 557,656,992 |
| Equipment | 44,596,989 | 2,573,025 | (2,411,912) | 44,758,102 |
| Other improvements | 235,597,001 | 12,347,906 | - | 247,944,907 |
| Total depreciable business-type assets | 2,286,674,176 | 134,039,640 | (12,505,804) | 2,408,208,012 |
| Accumulated depreciation | | | | |
| Infrastructure | (248,198,127) | (21,149,471) | - | (269,347,598) |
| Building & Improvement | (586,845,376) | (48,440,525) | 8,707,532 | (626,578,369) |
| Equipment | (25,297,644) | (3,517,672) | 1,998,296 | (26,817,020) |
| Other improvements | (116,663,770) | (9,049,054) | - | (125,712,824) |
| Total accumulated depreciation | (977,004,917) | (82,156,722) | 10,705,828 | (1,048,455,811) |
| Net depreciable business type assets | 1,309,669,259 | 51,882,918 | (1,799,976) | 1,359,752,201 |
| Total business type assets | \$ 1,474,347,827 | \$ 250,140,771 | \$ (128,086,591) | \$ 1,596,402,007 |

A portion of bond interest expense net of related interest income on unexpended funds is capitalized during the construction phase of the projects funded by the bonds. Net interest capitalized to construction in progress was \$11,428,200 for the fiscal year, which represents \$20,092,626 in interest expense net of \$8,664,626 of related interest income. Depreciation and amortization expense for the year was \$82,156,722.

5. DEFERRED REVENUE

Deferred revenue of \$15,390,422 includes revenues received in advance, excess billing to the scheduled airlines, and credit balance receivables at June 30, 2009.

6. ARBITRAGE REBATE

The Aviation Fund has several series of revenue bonds subject to federal arbitrage requirements. Federal tax legislation requires that the accumulated net excess of interest income on these issues over interest expense paid on the bonds be paid to the federal government at the end of a five year period. The arbitrage rebate liability as of June 30, 2009 was \$1,332,148 and is included in other long-term liabilities.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

7. INTEREST RATE SWAP

Objective: In April 2002, the City entered into a swaption that provided the City's Aviation Department (the Philadelphia Airport) with an up-front payment of \$6.5 million. As a synthetic refunding of its 1995 Bonds, this payment approximated the present-value savings as of April, 2002, of refunding on June 15, 2005, based upon interest rates in effect at the time. The swaption gave JP Morgan Chase Bank, N.A. the option to enter into an interest rate swap with the Airport whereby JP Morgan would receive fixed amounts and pay variable amounts.

Terms: JP Morgan exercised its option to enter into a swap on June 15, 2005, and the swap commenced on that date. Under the swap, the Airport pays multiple fixed swap rates (starting at 6.466% and decreasing over the life of the swap to 1.654%). The payments are based on an amortizing notional schedule (with an initial notional amount of \$189.5 million) and when added to an assumption for remarketing, liquidity costs and cost of issuance were expected to approximate the debt service of the refunded bonds at the time the swaption was entered into. The swap's variable payments are based on the SIFMA Municipal Swap Index. If the rolling 180-day average of the SIFMA Municipal Swap Index exceeds 7.00%, JP Morgan Chase has the option to terminate the swap.

As of June 30, 2009, the swap had a notional amount of \$173.9 million and the associated variable-rate bonds had a \$173.9 million principal amount. The bonds' variable-rate coupons are not based on an index but on remarketing performance. The bonds mature on June 15, 2025. The swap will terminate on June 15, 2025 if not previously terminated by JP Morgan Chase.

Fair Value: As of June 30, 2009, the swap had a negative fair value of (\$28.5 million). This means that if the swap terminated today, the Airport would have to pay this amount to JP Morgan Chase.

Risk: As of June 30, 2009, the Airport was not exposed to credit risk because the swap had a negative fair value. Should interest rates change and the fair value of the swap become positive, the Airport would be exposed to credit risk in the amount of the swap's fair value. In addition, the Airport is subject to basis risk should the relationship between SIFMA and the bonds change; if SIFMA resets at a rate below the variable bond rate, the synthetic interest rate will be greater than anticipated. The swap includes an additional termination event based on downgrades in credit ratings. The swap may be terminated by the Airport if JP Morgan's ratings fall below A- or A3, or by JP Morgan Chase if the Airport's ratings fall below BBB or Baa2. No termination event based on the Airport's ratings can occur as long as MBIA is rated at least A- or A3. MBIA is currently below this rating level.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

As of June 30, 2009, the rates were:

| <u>Interest Rate Swap</u> | <u>Terms</u> | <u>Rates</u> |
|------------------------------------|---------------|------------------------|
| Fixed payment to JPMorgan Chase | Fixed | 5.87072% |
| Variable rate from JPMorgan Chase | SIFMA | <u>-0.35000%</u> |
| Net interest rate swap payments | | 5.52072% |
| Variable rate bond coupon payments | Weekly resets | <u>0.40000%</u> |
| Synthetic interest rate on bonds | | <u><u>5.92072%</u></u> |

Swap payments and associated debt: As of June 30, 2009, debt service requirements of the variable-rate debt and net swap payments for their term, assuming current interest rates remain the same, were as follows:

| <u>Fiscal Year</u> <u>Ending June 30</u> | <u>Variable Rate Bonds</u> | | <u>Interest Rate</u> <u>Swaps Net</u> | <u>Total</u> <u>Interest</u> |
|---|----------------------------|---------------------|--|---------------------------------|
| | <u>Principal</u> | <u>Interest</u> | | |
| 2010 | \$ 5,300,000 | \$ 695,600 | \$ 9,600,532 | \$ 10,296,132 |
| 2011 | 6,000,000 | 674,400 | 9,307,934 | 9,982,334 |
| 2012 | 6,700,000 | 650,400 | 8,976,691 | 9,627,091 |
| 2013 | 7,500,000 | 623,600 | 8,606,802 | 9,230,402 |
| 2014 | 8,200,000 | 593,600 | 8,192,748 | 8,786,348 |
| 2015 - 2019 | 53,100,000 | 2,411,200 | 33,278,900 | 35,690,100 |
| 2020 - 2024 | 71,300,000 | 1,195,000 | 16,501,432 | 17,696,432 |
| 2025 | <u>15,800,000</u> | <u>63,200</u> | <u>872,274</u> | <u>935,474</u> |
| | <u>\$ 173,900,000</u> | <u>\$ 6,907,000</u> | <u>\$ 95,337,313</u> | <u>\$ 102,244,313</u> |

8. BONDS PAYABLE

General obligation (G.O.) bonds, payable out of Aviation Fund revenues, consist of bonds declared by statute to be self-sustaining from airport revenues. There are no G.O. bonds outstanding as of June 30, 2009.

In July 1997, Airport Revenue Refunding Bonds, Series 1997A in the amount of \$123,565,000 were issued. The proceeds of Series 1997A were used to: refund the City's Airport Revenue Bonds, Series 1978, Series 1984, and Series 1985; fund the deposit into the sinking fund reserve; and pay costs of issuance relating to the bonds.

In March 1998, Airport Revenue Refunding Bonds, Series 1998A in the amount of \$123,405,000 were issued. The proceeds of these bonds were used to refund the City's Airport Revenue Bonds, Series 1988; fund the deposit into the sinking fund reserve; and pay costs of issuance relating to the bonds.

CITY OF PHILADELPHIA
AVIATION FUND

Notes to Financial Statements
June 30, 2009

In July 1998, Airport Revenue Bonds, Series 1998B in the amount of \$443,700,000 were issued. The proceeds of Series 1998B were used to prepay the City's fixed rental obligation under a lease with PAID ("the PAID Lease"). Under this lease, the City acquired a leasehold interest and will occupy, operate and manage certain new terminals and related improvements ("the US Airways Project Facility") constructed with funds provided by the Series 1998A PAID Airport Revenue Bonds.

In July 2001, Airport Revenue Bonds, Series 2001A in the amount of \$187,680,000 were issued. The proceeds of Series 2001A were used to prepay an additional fixed rental obligation under the PAID Lease, attributable to completion costs of the US Airways Project Facility.

In July 2001, Airport Revenue Bonds, Series 2001B in the amount of \$40,120,000 were issued. The proceeds of Series 2001B were used to finance certain capital improvements to the airport system; fund the deposits into the sinking funds; finance capitalized interest; and pay costs of issuance relating to the bonds.

In June 2005, Airport Revenue Refunding Bonds, Series 2005C in the amount of \$189,500,000 were issued. The proceeds of Series 2005C were used to refund \$183,900,000 of the 1995A Series Airport Revenue Bonds, maturing from 2006 through 2025, and to pay issuance and insurance costs on the bonds. The cash flow required by the new bonds was the same as the cash flow required by the refunded bonds at the time of the sale. JPMorgan entered into a swaption agreement with the Airport on the 1995A bonds in 2002, which agreement was exercised June 15, 2005. In December 2008, the outstanding balance of \$178.6 million of Airport Revenue Refunding Bonds, Series 2005C was remarketed under an irrevocable direct pay letter of credit ("LOC") from TD Bank ("the Bank"). The LOC replaces a bond insurance policy from MBIA Insurance Corporation and a liquidity facility for the 2005C bonds provided by JP Morgan Chase Bank, N.A., pursuant to a standby bond purchase agreement, issued simultaneously with the issuance of the 2005C bonds in June 2005, and the surety policy for the sinking fund reserve account for the 2005C bonds. The LOC constitutes both a credit facility and liquidity facility under the Ordinance and the Variable Rate Securities Agreement, and the TD Bank will be the credit provider and liquidity provider under the Ordinance and the Variable Rate Securities Agreement for the 2005C bonds. The bonds have a weekly interest rate and maturity date in 2025.

In August 2005, Airport Revenue Bonds, Series 2005A sub-series (1), (2) and (3) in the amounts of \$59,860,000, \$22,575,000 and \$42,550,000, respectively, were issued. The proceeds of Series 2005A were used to finance a portion of the cost of Airport capital projects. Sub-series (1) are serial bonds and sub-series (2) and (3) are term bonds. The Series 2005A bonds had MBIA Insurance Corporation surety policies for their sinking fund reserve requirements. Because MBIA was downgraded below the 'AA' category, the surety policies no longer met the requirements of the Ordinance. During Fiscal 2009, the Aviation Fund replaced the surety policy by cash-funding the sinking fund reserve required under the Bond Ordinance.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

In August 2007, Airport Revenue Bonds, Series 2007A in the amount of \$172,470,000 were issued. The proceeds of Series 2007A were used to finance a portion of the 2007 Project (infrastructure improvements and design of terminal building enhancements), finance capitalized interest during the construction period and to pay the costs of issuing and insuring the bonds with municipal bond insurance and a surety policy.

In August 2007, Airport Revenue Bonds, Refunding Series 2007B in the amount of \$82,915,000 were issued. The proceeds of Series 2007B were used to refund Revenue Bonds, Series 1997B and the costs of issuing and insuring the bonds with municipal bond insurance. The refunding structure of the 2007B bonds realized a net present value savings of approximately \$2.6 million or 3.22% of the principal amount of the refunded bonds. The early extinguishment of debt resulted in an accounting loss of approximately \$3.2 million, representing the difference between the reacquisition price of \$83.1 million and the amount of debt extinguished of \$81.4 million (less \$1.5 million unamortized discount). The resulting loss will be amortized over the life of the refunded bonds through 2027.

In April 2009, Airport Revenue Bonds, Refunding Series 2009A sub series (1) through (3) in the amount of \$45,715,000 were issued. Serial bonds were issued in the amount of \$25.7 million with interest rates ranging from 1.5% to 5.0% maturing in 2023. Term bonds were issued in the amount of \$3.9 million and \$16.1 million with interest rates ranging from 5.0% to 5.375% maturing in 2024 and 2029 respectively. The gain/loss on the bonds cannot be calculated in the usual way because the refunded bonds (series 2005B) were variable rate bonds that were subject to Alternative Minimum Tax (AMT). However the 2009A bonds were issued on a fixed rate basis and are not subject to AMT. The proceeds of Series 2009A along with other monies of the Aviation Fund were used to currently refund Airport Revenue Bonds Series 2005B, fund a deposit to the parity sinking fund reserve account in respect of the bonds, and pay the costs of issuance of the bonds. The Series 2009A bonds were issued under a financial guaranty insurance policy issued by Assured Guaranty Corp. The early extinguishment of debt resulted in a loss on refunding of approximately \$1 million, representing the unamortized discount on the bonds. The resulting loss will be amortized over the life of the refunded bonds, through 2023.

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

The amount of debt service payable for revenue bonds to maturity is as follows:

| Years Ending | Total | | |
|--------------|-------------------------|-----------------------|-------------------------|
| June 30 | Principal | Interest | Debt Service |
| 2010 | \$ 38,510,000 | \$ 65,744,897 | \$ 104,254,897 |
| 2011 | 45,855,000 | 63,277,697 | 109,132,697 |
| 2012 | 48,555,000 | 60,502,416 | 109,057,416 |
| 2013 | 51,510,000 | 57,553,279 | 109,063,279 |
| 2014 | 54,490,000 | 54,579,582 | 109,069,582 |
| 2015-2019 | 284,960,000 | 224,274,876 | 509,234,876 |
| 2020-2024 | 311,770,000 | 148,056,159 | 459,826,159 |
| 2025-2029 | 311,775,000 | 71,648,528 | 383,423,528 |
| 2030-2034 | 83,775,000 | 22,216,275 | 105,991,275 |
| 2035-2039 | 40,010,000 | 3,636,413 | 43,646,413 |
| Total | <u>\$ 1,271,210,000</u> | <u>\$ 771,490,122</u> | <u>\$ 2,042,700,122</u> |

The early extinguishment of debt can result in a loss on refunding, representing the difference between the reacquisition price, plus unamortized premium, discount and issuance costs, and the amount of debt extinguished. The resulting loss is amortized annually over the life of the refunded bonds.

Total interest cost for the fiscal year was \$72,178,174 of which \$20,092,626 was capitalized and \$52,085,548 was recorded as non-operating expense.

Details of the various revenue bonds included in the financial statements are reflected on the following page. Airport Revenue Bonds Series 1998B and 2001A reflect the PAID outstanding balances, which are treated as conduit debt under GASB Interpretation 2. Payments on the conduit debt are guaranteed by General Airport Revenue Bonds Series 1998B and 2001A.

CITY OF PHILADELPHIA
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Notes to Financial Statements
For the Year Ended June 30, 2009

8. BONDS PAYABLE

| Type of Debt | Description | Authorized and Issued | Included in Current Liabilities | Portion Due After June 30, 2010 | Total Outstanding Bonded Debt | Final Maturity | Interest Percentage Rate |
|--------------------------------------|-------------|-----------------------------|---------------------------------------|---------------------------------------|-------------------------------------|-------------------|--------------------------------|
| Airport Revenue Bonds - Series 1997A | Loan # 705 | \$ 123,565,000 | \$ 4,440,000 | \$ 26,130,000 | \$ 30,570,000 | 2015 | 5.00 - 6.00% |
| Airport Revenue Bonds - Series 1998A | Loan # 705 | \$ 123,405,000 | 6,425,000 | 65,540,000 | 71,965,000 | 2016 | 5.25 - 6.00% |
| Airport Revenue Bonds - Series 1998B | Loan # 706 | \$ 443,700,000 | 11,210,000 | 366,610,000 | 377,820,000 | 2028 | 4.25 - 5.38% |
| Airport Revenue Bonds - Series 2001A | Loan # 707 | \$ 187,680,000 | 4,670,000 | 159,555,000 | 164,225,000 | 2028 | 4.00 - 5.50% |
| Airport Revenue Bonds - Series 2001B | Loan # 708 | \$ 40,120,000 | 895,000 | 34,560,000 | 35,455,000 | 2031 | 4.00 - 5.25% |
| Airport Revenue Bonds - Series 2005C | Loan # 710 | \$ 189,500,000 | 5,300,000 | 168,600,000 | 173,900,000 | 2025 | Variable Rate |
| Airport Revenue Bonds - Series 2005A | Loan # 711 | \$ 124,985,000 | 2,460,000 | 120,185,000 | 122,645,000 | 2035 | 4.50 - 5.00% |
| Airport Revenue Bonds - Series 2007A | Loan # 712 | \$ 172,470,000 | | 172,470,000 | 172,470,000 | 2037 | 5.00 - 5.00% |
| Airport Revenue Bonds - Series 2007B | Loan # 713 | \$ 82,915,000 | 3,105,000 | 73,345,000 | 76,450,000 | 2027 | 4.50 - 5.00% |
| Airport Revenue Bonds - Series 2009A | Loan # 714 | \$ 45,715,000 | 5,000 | 45,705,000 | 45,710,000 | 2029 | 1.50 - 5.00% |
| | | | <u>\$ 38,510,000</u> | <u>\$ 1,232,700,000</u> | <u>\$ 1,271,210,000</u> | | |

Airport General Obligation Bonds authorized and unissued at June 30, 2009

\$ 62,500,000

CHANGES IN LONG-TERM DEBT:

| | Beginning Balance | Additions | Retirements/ Repayments | Ending Balance | Due Within One Year |
|---|-------------------------|----------------------|----------------------------|-------------------------|------------------------|
| Revenue bonds | \$ 1,302,800,000 | \$ 45,715,000 | \$ (77,305,000) | \$ 1,271,210,000 | \$ 38,510,000 |
| Less unamortized premium/ discount and loss on refunding | (20,415,795) | | | (20,415,795) | |
| Total bonds | 1,282,384,205 | 45,715,000 | (77,305,000) | 1,250,794,205 | 38,510,000 |
| Workers compensation claims | 3,783,860 | 2,702,783 | (1,141,043) | 5,345,600 | |
| Termination compensation payable | 6,049,096 | 1,125,406 | (633,176) | 6,541,326 | 684,700 |
| Legal liability | 50,000 | 1,673,958 | (430,737) | 1,293,221 | - |
| Arbitrage | 267,767 | 1,064,381 | | 1,332,148 | - |
| | <u>\$ 1,292,534,928</u> | <u>\$ 52,281,528</u> | <u>\$ (79,509,956)</u> | <u>\$ 1,265,306,500</u> | <u>\$ 39,194,700</u> |

CITY OF PHILADELPHIA
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Notes to Financial Statements
June 30, 2009

9. FUND BALANCES

The following is a description of the restrictions for all net assets categories of the Aviation Fund:

- *Invested in Capital Assets, Net of Related Debt* reflects the investment in fixed assets net of accumulated depreciation and offset by debt service related to expended bond proceeds.
- *Restricted for Capital Projects* reflects the unexpended funds from bond proceeds and PFCs, which are reserved for construction of capital projects.
- *Restricted for Debt Service* reflects the unexpended funds from bond proceeds and PFCs, which are reserved for repayment of debt.
- *Unrestricted* reflects net assets available for current and future operations.

10. PENSION PLAN

The Aviation Fund contributes to the Municipal Pension Plan (City Plan) of the City of Philadelphia. Information for the City Plan as a whole is available in the Comprehensive Annual Financial Report (CAFR) of the City of Philadelphia for the year ended June 30, 2009. Required Supplementary Information is presented in the audited financial statement of the City Plan, which may be obtained from the Director of Finance of the City of Philadelphia.

Plan Description

The Philadelphia Home Rule Charter (the Charter) mandates that the City maintain an actuarially sound pension and retirement system. To satisfy that mandate, the City's Board of Pensions and Retirement maintains the single-employer Municipal Pension Plan (the Plan). The Plan covers all officers and employees of the City and officers and employees of five other governmental and quasi-governmental organizations. By authority of two ordinances and related amendments passed by City Council, the Plan provides retirement benefits as well as death and disability benefits. Benefits vary by the class of employee. The Plan has two major classes of members – those covered under the 1967 Plan and those covered under the 1987 Plan. Both plans have multiple divisions.

CITY OF PHILADELPHIA
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Notes to Financial Statements
June 30, 2009

Retirement Benefits

An employee who meets the age and service requirements of the particular division in which he participates is entitled to an annual benefit, payable monthly for life, equal to the employee's average final compensation multiplied by a percentage that is determined by the employee's years of credited service. The formula for determining the percentage is different for each division. If fund earnings exceed the actuarial assumed rate by a sufficient amount, an enhanced benefit distribution to retirees, their beneficiaries, and their survivors shall be considered. A deferred vested benefit is available to an employee who has 10 years of credited service, has not withdrawn contributions from the system, and has attained the appropriate service retirement age. Members of both plans may opt for early retirement with a reduced benefit. The Deferred Retirement Option Plan (DROP) was initiated on October 1, 1999. Under this plan employees that reach retirement age may accumulate their monthly service retirement benefit in an interest bearing account at the Board of Pensions for up to four (4) years and continue to be employed by the City of Philadelphia.

Death Benefits

If an employee dies from the performance of duties, his/her spouse, children or dependent parents may be eligible for an annual benefit ranging from 15% to 80% of the employee's final average compensation. Depending on age and years of service, the beneficiary of an employee who dies other than from the performance of duties will be eligible for either a lump sum benefit only or a choice between a lump sum and an annual pension.

Disability Benefits

Employees disabled during the performance of duties are eligible for an immediate benefit equal to contributions plus a yearly benefit. If the employee subsequently becomes employed, the benefit is reduced by a percentage of the amount earned. Certain employees who are disabled other than during the performance of duties are eligible for an ordinary disability payment if they apply for the benefit within one year of termination. If the employee subsequently becomes employed, the benefit is reduced by a percentage of the amount earned.

Membership

Membership in the plan for the City as a whole as of July 1, 2008 was as follows:

| | |
|--|----------------------|
| Retirees and beneficiaries currently receiving benefits | 35,405 |
| Terminated members entitled to benefits but not yet receiving benefits | 1,263 |
| Active members | <u>29,215</u> |
| Total Members | <u><u>65,883</u></u> |

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

Funding Policy

Employee contributions are required by City Ordinance. For 1967 Plan members, employees contribute 3¾ % of their total compensation that is subject to FICA and 6% of compensation not subject to FICA. 1987 Plan contribution rates are defined for the membership as a whole by Council Ordinance. Rates for individuals are then determined annually by the actuary so that total individual contributions satisfy the overall rate set by Council.

The City is required to contribute the remaining amounts necessary to fund the Plan, using an acceptable actuarial basis as specified by the Home Rule Charter, City Ordinance and State Statute. Court decisions require that the City’s annual employer contributions are sufficient to fund:

- The accrued actuarially determined normal costs.
- Amortization of the unfunded actuarial accrued liability determined as of July 1, 1985. The portion of that liability attributable to a class action lawsuit by pension fund beneficiaries (the Dombrowski suit) is amortized in level installments, including interest, over 40 years through June 30, 2009. The remainder of the liability is amortized over 34 years with increasing payments expected to be level as a percentage of each year's aggregate payroll.
- Amortization in level dollar payments of the changes to the July 1, 1985 liability due to the following causes over the stated period:
 - non-active members’ benefit modifications (10 years)
 - experience gains and losses (15 years)
 - changes in actuarial assumptions (20 years)
 - active members’ benefit modifications (20 years)

Under the City’s current funding policy, the total required employer contribution for the current year amounted to \$524.1 million or 35.4% of covered payroll of \$1,462.5 million for the City as a whole. The City’s actual contribution was \$440.0 million, which met the Minimum Municipal Obligation as required by the Commonwealth of Pennsylvania’s Acts 205 and 189. The annual pension cost and related percentage contributed for the three most recent fiscal years for the Aviation Fund are as follows:

| <u>Year Ended</u> <u>June 30</u> | <u>Annual</u> <u>Pension Cost</u> | <u>Percentage</u> <u>Contributed</u> | <u>Net Pension</u> <u>Obligation</u> |
|-------------------------------------|--------------------------------------|---|---|
| 2007 | \$17,097,141 | 83.9% | \$(16,607,899) |
| 2008 | \$19,400,959 | 79.6% | \$(11,836,075) |
| 2009 | \$20,889,105 | 84.0% | \$ (8,099,111) |

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The actuarial valuation used to compute the current year's required contribution was performed as of July 1, 2008. Methods and assumptions used for that valuation include:

- the individual entry age actuarial cost method
- a five-year smoothed market value method for valuing investments
- a level percentage closed method for amortizing the unfunded liability
- an annual investment rate of return of 8.75%
- projected annual salary increases of 5.0% (including inflation)
- annual inflation of 2.75%
- no post-retirement benefit increases

Administrative costs are funded out of the Plan's assets.

Funding Status

The following schedule shows the funding status based on the latest actuary report for the City as a whole. The schedule of funding progress, which presents multiyear trend information about whether the actuarial value of the plan assets is decreasing over time relative to the actuarial accrued liability for benefits, can be found in the Required Supplementary Information section of the CAFR.

| (in millions) | | | | | | UAAL as a |
|---------------|---------------|------------------------|---------------|--------------|----------------|----------------|
| Actuarial | Actuarial | Actuarial | Unfunded | Funded | Covered | Percent of |
| Valuation | Value of | Accrued | AAL | Ratio | Payroll | Covered |
| <u>Date</u> | <u>Assets</u> | <u>Liability (AAL)</u> | <u>(UAAL)</u> | <u>Ratio</u> | <u>Payroll</u> | <u>Payroll</u> |
| 7/1/2008 | \$ 4,623.6 | \$ 8,402.2 | \$ 3,778.6 | 55.03% | \$ 1,456.5 | 259.43% |

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

Net Pension Obligation

The City and other employers' annual pension cost and net pension obligation (NPO) for the Plan for the current year were as follows:

| | (in thousands) |
|--|----------------|
| Annual Required Contribution (ARC) | \$ 539,464 |
| Interest on Net Pension Obligation (NPO) | (48,957) |
| Adjustment to ARC | 68,399 |
| Annual Pension Cost | 558,906 |
| Contributions Made | (455,389) |
| Increase in NPO | 103,517 |
| NPO at Beginning of Year | (559,505) |
| NPO at End of Year | \$ (455,988) |
| Interest Rate | 8.75% |
| 15 Year Amortization Factor (EOY) | 8.18% |

The required employer contribution for the Aviation Fund was 34.4% of covered payroll of \$60.8 million.

Summary of Significant Accounting Policies

Financial statements of the Plan are prepared using the accrual basis of accounting. Contributions are recognized as revenues when due, pursuant to formal commitments, as well as statutory or contractual requirements. Benefits and refunds paid are recognized when due and payable in accordance with the terms of the plan.

The Municipal Pension Fund issues a separate annual financial report. To obtain a copy, contact the Director of Finance of the City of Philadelphia.

11. OTHER POST EMPLOYMENT BENEFITS (OPEB)

The following information is provided for the City as a whole because discrete information is not available for the Aviation Fund.

Plan description: The City of Philadelphia self-administers a single-employer, defined benefit plan and provides health care for five years subsequent to separation for eligible retirees. Certain union represented employees may defer their coverage until a later date but the amount that the City pays for their health care is limited to the amount that the City would have paid at the date of their retirement. The City also provides lifetime insurance coverage for all eligible retirees. Firefighters are entitled to \$7,500 coverage and all other employees receive \$6,000 in coverage. The Plan does not issue stand-alone

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financial statements, and the accounting for the plan is reported within the financial statements of the City of Philadelphia.

Funding Policy: The City funds its' retiree benefits on a pay-as-you-go basis. To provide health care coverage, the City pays a negotiated monthly premium for retirees covered by union contracts or pays the health care providers directly for non-unionized employees. For fiscal year 2009, the City paid \$76.6 million for retiree healthcare.

Annual OPEB Cost and Net OPEB Obligation: The City's annual other post employment benefit (OPEB) expense is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding, which if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty (30) years. The following table shows the components of the City's annual OPEB cost for the year, the amount actually contributed to the plan and changes in the net OPEB obligation:

| | (in thousands) |
|---|-------------------------|
| Annual required contribution | \$ 98,697 |
| Interest on net OPEB obligation | 183 |
| Adjustment to ARC | (147) |
| Annual OPEB cost | <u>98,733</u> |
| Payments made | <u>(81,251)</u> |
| Increase in net OPEB obligation | 17,482 |
| Net OPEB obligation – beginning of year | <u>3,668</u> |
| Net OPEB obligation – end of year | <u><u>\$ 21,150</u></u> |

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for the two most recent fiscal years was as follows:

| Amounts in thousands | | | |
|--------------------------|---------------------|--------------------------------------|------------------------|
| Year Ended June 30 | Annual OPEB Cost | Percentage of OPEB Contributed | Net OPEB Obligation |
| <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| 2008 | \$ 83,373 | 96.0% | \$ 3,668 |
| 2009 | \$ 98,733 | 82.0% | \$ 21,150 |

CITY OF PHILADELPHIA
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Funded Status and Funding Progress: As of July 1, 2008, the most recent actuarial valuation date, the City is funding OPEB on a pay as you go basis and accordingly, the unfunded actuarial accrued liability (UAAL) for benefits was \$1.2 billion. The covered annual payroll was \$1.5 billion and the ratio of the UAAL to the covered payroll was 79.0 percent.

The required schedule of funding progress, presenting the multi-year trend information about the actuarial value of the plan assets relative to the actuarial accrued liability, is contained in the comprehensive annual financial report of the City of Philadelphia.

The projections of future benefit payments for an ongoing plan obligation involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Amounts determined regarding the funded status of the obligation and contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Actuarial Methods and Assumptions: Projections of costs for financial reporting purposes are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing costs between the employer and the plan members.

Costs were determined according to the individual entry age actuarial cost method with the attribution period ending at each decrement age. This is consistent with the cost method used for the City of Philadelphia Municipal Retirement System. Unfunded liabilities are funded over a 30 year period as a level percentage of payroll, which is assumed to increase at a compound annual rate of 4% per year. The actuarial assumption included a 3.5% compound annual interest rate on the City's general investments.

12. DEFERRED COMPENSATION PLAN

The City offers its employees a deferred compensation plan in accordance with the Internal Revenue Service Code section 457. As required by the Code and Pennsylvania laws in effect at June 30, 2009, the assets of the plan are held in trust for the exclusive benefit of the participants and their beneficiaries. In accordance with GASB #32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*, the Aviation Fund does not include the assets or activity of the plan in its financial statements.

CITY OF PHILADELPHIA
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Notes to Financial Statements
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13. ACCUMULATED UNPAID SICK LEAVE

The Aviation Fund follows City policies regarding accumulation of sick leave. City employees may accumulate unused sick leave to predetermined balances. The accumulated sick leave is payable in varying amounts from 25% to 50% only upon retirement or in some cases death while on active duty. The City budgets for, and charges, the cost of sick leave as it is taken.

14. OPERATING LEASES

The Aviation Fund as a Lessor

The City and the participating airlines executed a new 4 year Airport-Airline Use and Lease Agreement effective July 1, 2007. The Airline Agreement employs a residual cost center approach, wherein airline rates and charges are calculated to fund the annual net expense of PHL's airfield and terminal facilities after taking into account non-airline revenues generated by the Airport. The rate-making provisions of the new agreement also provide for the creation and funding of Airport budgetary reserves to enhance PHL's financial capacity and flexibility.

The Aviation Fund's other operating leases consist primarily of leases of airport facilities for retail or other aviation related matters. Most assets constructed by lessees under terms of the lease revert to the City at the end of the lease term. Those assets are recorded at fair value, as determined by an appraisal on the property. During fiscal 2009, the Aviation Fund acquired capital improvements, with a fair value of \$5.2 million at the end of the lease term, from the car rental companies.

The Aviation Fund's most significant non-airline lease is with MarketPlace Philadelphia, LP for the development and management of the food and retail program throughout Philadelphia International Airport. The award-winning food and retail program consists of 157 shops, restaurants, retail carts and passenger services throughout Terminals A-West through F. The lease agreement provides for MarketPlace Philadelphia, LP to pay rentals to the City in the form of minimum annual guarantees and profit sharing.

Rental income from operating leases for the year was as follows:

| | |
|---------------------|----------------|
| Minimum rentals | \$ 27,254,113 |
| Additional rentals | 148,747,500 |
| | <hr/> |
| Total rental income | \$ 176,001,613 |
| | <hr/> <hr/> |

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

As of year-end, future minimum rentals receivable under non-cancelable operating leases are as follows:

| Years Ending June 30 | Future Payments |
|-------------------------|--------------------|
| 2010 | \$ 18,608,040 |
| 2011 | 14,582,548 |
| 2012 | 13,576,983 |
| 2013 | 13,176,974 |
| 2014 | 7,045,137 |
| 2015-2019 | 31,292,856 |
| 2020-2024 | 18,962,530 |
| 2025-2029 | 12,366,375 |
| 2030-2034 | 10,320,051 |
| Total | \$ 139,931,494 |

The separate cost and carrying amount of property held for leasing is not available.

The Aviation Fund as a Lessee

The Aviation Fund leases office space, land, and both office and operations equipment on short-term and long-term bases. Rental expense for operating leases for the year was as follows:

| | |
|---------------------|---------------|
| Minimum rentals | \$ 1,906,385 |
| Additional rentals | 10,559,050 |
| Total rental income | \$ 12,465,435 |

CITY OF PHILADELPHIA
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Notes to Financial Statements
June 30, 2009

As of year-end, future minimum rental commitments for operating leases having initial or remaining non-cancelable lease terms of more than one year are as follows:

| Years Ending June 30 | |
|-------------------------|---------------------|
| 2010 | \$ 1,677,684 |
| 2011 | 1,063,716 |
| 2012 | 771,578 |
| 2013 | 491,844 |
| 2014 | 90,530 |
| 2015-2019 | 45,265 |
| Total | <u>\$ 4,140,617</u> |

15. RISK MANAGEMENT

The Aviation Fund is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Aviation Fund is self-insured for worker's compensation and unemployment compensation and insured through insurance carriers for other coverage.

The City covers all claim settlements and judgments, except those discussed above, out of the resources of the fund associated with the claim. Claims liabilities and expenditures are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported; the effects of specific incremental claims adjustment expenditures, salvage and subrogation; and unallocated claims adjustment expenditures.

At June 30, the amount of these liabilities for the City as a whole was \$309.3 million. This liability is the City's best estimate based on available information. Changes in the reported liability since June 30, 2007 resulted from the following:

| (in millions) | Beginning Liability | Current Year Claims and Changes in Estimates | Claim Payments | Ending Liability |
|---------------|------------------------|---|-------------------|---------------------|
| Fiscal 2008 | \$275.9 | \$74.2 | \$(89.0) | \$261.1 |
| Fiscal 2009 | \$261.1 | \$144.4 | \$(96.2) | \$309.3 |

The City's unemployment and workers' compensation coverages are provided through its general fund and are funded by a pro-rata charge to the various funds. The City's payments for the year were \$4.2 million for unemployment compensation claims and \$55.5 million for workers' compensation claims.

CITY OF PHILADELPHIA
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The City's estimated outstanding workers' compensation liabilities are \$267.3 million discounted at 3.5% and \$339.1 million on an undiscounted basis. These liabilities include provisions for indemnity, medical and allocated loss adjustment expense (ALAE). Excluding the ALAE, the respective liabilities for indemnity and medical payments relating to workers compensation total \$244.7 million discounted and \$311.6 million undiscounted. The Aviation Fund's accrued liability for worker's compensation was \$5,345,600 at June 30, 2009. Further discrete information is not available for the Aviation Fund.

During the last three (3) fiscal years, no claim settlements have exceeded the level of insurance coverage for operations using third party carriers. None of the City's insured losses have been settled with the purchase of annuity contracts.

16. CONCENTRATION OF CREDIT RISK

US Airways is the principal airline serving Philadelphia International Airport. For Fiscal 2009, the airline, together with its US Airways Express affiliates accounted for approximately 64.3% of passengers enplaned at the airport. Operating revenues from US Airways and its affiliates totaled approximately \$110.0 million in Fiscal Year 2009, which represented approximately 44.0 % of total Aviation Fund operating revenues.

17. CONTINGENCIES AND COMMITMENTS

As of June 30, 2009, the Aviation Fund had commitments of approximately \$31.9 million for operating expenses and \$229.7 million for capital assets and improvements. The Aviation Fund expects to fund these commitments through operations and through capital grants, bond proceeds, and passenger facility charges.

Litigation

Condemnation of Tract of Land k/a Parcel C (within Eastwick Urban Renewal Area): In November 2003, the City condemned certain property known as parcel C within the Eastwick Urban Renewal Area Plan of 1958 for the benefit of Philadelphia International Airport. The Redevelopment Authority of the City of Philadelphia (RDA) was the record title holder for the property. The City deposited in court estimated just compensation in the amount of \$7.7 million. In 2007, Eastwick Development Joint Venture IX, L.P. and New Eastwick Corporation, petitioned the Court for appointment of a Board of Viewers and the Court appointed a Board of View to ascertain and award just compensation. Eastwick alleged they owned or held equitable interest in and certain development rights to the condemned property. After a view of the premises and a hearing in July 2009, the Board filed a report with the Court and made an award of just compensation for the property of \$13.5 million (including attorney fees), subject to credit for the \$7.7 million already paid and distributed. In addition, the Board awarded delay damages from the date of taking (November 2003) until July 2009 in the amount of \$3.3 million and

CITY OF PHILADELPHIA
AVIATION FUND
Notes to Financial Statements
June 30, 2009

accruing interest thereafter until payment at the rate of 4.25% per year through 2009, and at rates not yet fixed for subsequent years.

The City filed an appeal to the Court of Common Pleas in November 2009, requesting a jury trial de novo. The City objected, among other things, to the award of any compensation amount beyond that amount already paid into court, to evidentiary, procedural and substantive errors in the Board of View proceeding and award, and to delay damage computation and award. Eastwick Development filed a separate appeal from the Board of View Report to the Court of Common Pleas in November 2009. Eastwick Development sought a jury trial de novo and objected to the sufficiency of the amount of compensation awarded. The Court scheduled a case management conference for the cases in February 2010.

The City vigorously contests the award. At this time, the City's attorneys are unable in their professional judgment to evaluate the likelihood of unfavorable outcome in terms of probability and the range or amount of any loss assuming an unfavorable outcome. Any ultimate judgment would be paid from the Aviation Fund.

CITY OF PHILADELPHIA

AVIATION FUND

Reconciliation of Fund Balance (Legally Enacted Basis) to

Net Assets (GAAP Basis)

For the Year Ended June 30, 2009

| | |
|---|------------------------|
| Fund balance, legal basis June 30, 2009 | \$ 55,127,876 |
| Add assets not included in legal basis: | |
| Current assets | 14,408,114 |
| Fixed assets, net of depreciation | 1,596,402,007 |
| Restricted assets | 433,326,337 |
| Net pension asset | 8,099,111 |
| | <u>2,052,235,569</u> |
| Deduct liabilities not included in legal basis: | |
| Construction accounts payable | (44,398,183) |
| Current liabilities | (24,031,818) |
| Bonds payable | (1,250,387,864) |
| Other long-term liabilities | (13,827,595) |
| | <u>(1,332,645,460)</u> |
| Add (deduct) fund balance accounts included in legal basis: | |
| Reserve for encumbrance, current | 81,706 |
| Reserve for encumbrance, prior | 23,011,276 |
| Reserve for collectible accounts | |
| | <u>23,092,982</u> |
| Net assets - GAAP basis, June 30, 2009 | <u>\$ 797,810,967</u> |

CITY OF PHILADELPHIA
AVIATION FUND
Budgetary Comparison Schedule
For the Fiscal Year Ended June 30, 2009
(Amounts in thousands)

| | <u>Budgeted Amounts</u> | | | <u>Final Budget to Actual Positive (Negative)</u> |
|--|-------------------------|--------------|---------------|---|
| | <u>Original</u> | <u>Final</u> | <u>Actual</u> | |
| <u>Revenues</u> | | | | |
| Locally Generated Non-Tax Revenue | \$342,166 | \$325,139 | \$291,282 | (\$33,857) |
| Revenue from Other Governments | 2,500 | 2,500 | 1,934 | (566) |
| Revenue from Other Funds | 1,500 | 2,000 | 887 | (1,113) |
| Total Revenues | 346,166 | 329,639 | 294,103 | (35,536) |
| <u>Expenditures and Encumbrances</u> | | | | |
| Personal Services | 67,653 | 67,619 | 60,892 | 6,727 |
| Pension Contributions | 19,270 | 20,852 | 20,852 | - |
| Other Employee Benefits | 18,637 | 19,056 | 18,656 | 400 |
| Sub-Total Employee Compensation | 105,560 | 107,527 | 100,400 | 7,127 |
| Purchase of Services | 99,475 | 99,498 | 78,973 | 20,525 |
| Materials and Supplies | 7,524 | 7,538 | 7,360 | 178 |
| Equipment | 5,786 | 5,785 | 2,352 | 3,433 |
| Contributions, Indemnities and Taxes | 4,512 | 2,510 | 938 | 1,572 |
| Debt Service | 114,021 | 114,021 | 99,676 | 14,345 |
| Payments to Other Funds | 25,423 | 25,423 | 12,780 | 12,643 |
| Total Expenditures and Encumbrances | 362,301 | 362,302 | 302,479 | 59,823 |
| Operating Surplus (Deficit) for the Year | (16,135) | (32,663) | (8,376) | 24,287 |
| Fund Balance Available for Appropriation, July 1, 2008 | 59,124 | 61,410 | 61,412 | 2 |
| <u>Operations in Respect to Prior Fiscal Years</u> | | | | |
| Commitments Cancelled - Net (Budget Book) | 15,000 | 12,000 | 2,092 | (9,908) |
| Adjusted Fund Balance, July 1, 2008 | 74,124 | 73,410 | 63,504 | (9,906) |
| Fund Balance Available for Appropriation, June 30, 2009 | \$57,989 | \$40,747 | \$55,128 | \$14,381 |