FINANCIAL FRAMEWORK FOR THE GRANT OF A TYPE "A" OPERATING LICENCE

In order for a company to operate aircraft for the carriage of passengers or cargo for remuneration it must meet a number of criteria set out in Council Regulation (EEC) 2407/92 on the licensing of air carriers. For applicants wishing to operate aircraft with 20 or more seats or weighing 10 or more tonnes, this includes the financial criteria set out in Article 5. This note sets out in outline the approach that the CAA typically takes when considering applications for Operating Licences in the light of paragraph 1 of that Article. It is possible that in some cases a different framework will be appropriate; this will be decided on a case by case basis.

Paragraph 1 of Article 5 requires that applicants have adequate funds to meet two separate tests. The CAA addresses this by analysing the applicant's business plan, to establish whether it is based on realistic assumptions and, if not, what the assumptions should be. Using the revised assumptions if necessary, the balance sheet and cash positions are projected forward for two years. If these projections suggest that the applicant does not have sufficient starting funds to meet the tests in Article 5, then the CAA may require more capital than proposed in the business plan. This paper will go on to describe in some detail how the funding requirement is set; in general terms a new airline will need enough funds to cover initial capital expenditure, including lease deposits, and other setting-up costs, as well as enough to cover initial losses. The following sections discuss:

- Section 1. The process involved in considering the financial aspects of the application, from receipt of the application to grant of a licence.
- Section 2. The approach that the CAA takes to the analysis of business plans.
- Section 3. The approach that the CAA takes to determining the level of funds available to the business.
- Section 4. The way in which the CAA interprets the tests in paragraph 1 of Article 5.

1. PROCESS OF CONSIDERING APPLICATION

The process will start with the CAA's analysis of the applicant's business plan. This is discussed in more detail in Section 2. In outline, this consists of considering each aspect of the plan against independent evidence, and using particular analytical techniques. In some cases this will suggest that the plan is optimistic; projected passenger numbers or yields may be high, or costs may be too low. In such cases the CAA will prepare an alternative version of the plan.

As the CAA's analysis progresses any key results will usually be communicated to the applicant, and it is of course open to the applicant to provide a response to the analysis, where it disagrees with the results.

The final decision on the funding required for the Operating Licence to be granted will be taken by the Board Member of the CAA with special responsibility for Licensing and Finance, following a meeting with the company. The Board Member's decision on the funding requirement will ultimately be based on his view of whether, using the CAA's framework of interpreting balance sheets and cash (see Section 3), the applicant meets the tests in Article 5, paragraph 1 (see Section 4).

However before the application can progress to that stage, the CAA will require evidence that funding is likely to be available to the applicant once a decision has been made. It is difficult to state precisely what constitutes sufficient evidence; in general terms, the applicant should be able to produce written evidence that persons or organisations, with sufficient financial strength, support the application and would be likely to invest in it.

Once the decision has been made, the applicant will be issued with a letter stating the conditions on which a licence will be granted. Among other conditions deriving from Council Regulation 2407/92 (such as adequate insurance and possession of an AOC) it is likely to indicate that the licence will be granted once the CAA has received written confirmation from the applicant's auditors that the appropriate level of funding has been injected into the company. It may include other requirements, such as signed copies of contracts or leases, depending on the nature of the application. Once all of the conditions have been met, the licence will be granted.

As indicated elsewhere in the pack, the CAA is obliged under the Citizens' Charter to produce a decision not more than two months after receiving all of the required information. It is important to remember that the two months does not start until the CAA has received all of the information it requires. In our experience it is rare for applicants' plans, and even their first responses, to include enough information for a decision to be reached. It would therefore be prudent for applicants to allow significantly longer than two months for this process.

2. CAA ANALYSIS OF BUSINESS PLANS

The application should be accompanied by financial information, comprising a business plan, actual and projected financial statements and other supporting documentation. The required information is specified in Appendix A to this paper.

In considering the applicant's prospects the CAA will consider whether the business plan is based on reasonable assumptions; this is referred to as the analysis of the business plan. The guiding principle behind this analysis is that the assumptions are most likely to be reasonable when they are borne out by independent evidence. The remainder of this section discusses most of the ways in which the CAA seeks such evidence. That is not to say that there are no other valid ways of forecasting, merely that the CAA is likely to assess an applicant's business plan using the following approaches. The analysis is likely to be less time consuming if the plan spells out the assumptions on which it based, and is accompanied by as much independent supporting evidence as possible.

While analysing the plan the CAA staff involved are likely to need to seek clarification from the applicant on particular points. In some cases the most time consuming part of an application is waiting for answers from the applicant. Since most applicants are interested in receiving an answer as soon as possible, it is in the applicant's own interests firstly to provide a plan which explains and supports their reasoning as fully as possible, and secondly to respond promptly to the CAA's requests for further information.

In some cases the CAA's view will be based on confidential data and in those cases we cannot indicate the reasons why the CAA view differs. For example, the applicant may intend to fly on a route which is already operated by an incumbent carrier. We may have actual average yield data on that route, and if the applicant's projected yield is higher then we might conclude that the projection was unrealistic. We could then communicate the conclusion to the applicant but as to the reasons for it we could only indicate that it derived from confidential data.

2.1 Scheduled Revenues

This typically splits into passenger numbers and yield, and the approaches used for these differ. Of course in reality there is a trade off and it is generally possible to deduce, by comparison with existing carriers, whether the level of yield expected is consistent with the passenger numbers.

2.1.1 Passenger Numbers

The CAA usually uses an approach based on a ratio called the Competitive Performance Index, or CPI. The CPI is simply the ratio, in a particular market, between an airline's market share and either its frequency share (CPI(F)) or capacity share (CPI(C)), depending on whether the route is more business or leisure oriented. It is useful because, in the absence of any specific reasons why it would change, the ratio tends to stay constant year-on-year. In considering the applicant's route, we will generally determine a suitable CPI by analogy with an existing carrier in similar circumstances, making adjustments as necessary. Then, after calculating the applicant's projected capacity or market share and estimating the market size it is possible to use this ratio to calculate the expected passenger numbers for a particular airline.

Selection of the CPI is judgmental and the necessary adjustments vary from case to case, depending on how close an analogy can be made with an existing carrier. The most common standard adjustment is for the learning curve; where the available CPIs are for established carriers, it is necessary to apply reductions for the newness of the carrier and the route. Based on its experience of the build-up of traffic in such circumstances, the CAA usually applies a reduction of 20% in passenger numbers in the first year of operation and 10% in the second.

The CAA sources of data on market size are listed in the blue note which forms part of this pack.

2.1.2 Yields

Again the CAA's approach is to look for carriers in similar circumstances, offering similar products, and compare their yields. Often the analogy is not perfect and adjustments must be made, for example to take account of a different business/leisure split on the applicant's and comparator's routes, or because one carrier presents itself as low-cost while the other offers a conventional service. As part of its role in monitoring the finances of Operating Licence holders the CAA receives yield data from existing carriers and this is its main source of information in this area. However this is a perfect example of information that the CAA cannot reveal to the applicant; we can reveal our conclusion but not our reasoning.

2.2 Charter Revenues

The treatment of charter revenues depends on how integrated the airline is with a particular tour operator. If, for example, the applicant is to be a wholly owned subsidiary of an existing tour operator, and proposes to make little by way of third party sales, then the question becomes whether the tour operator can sell enough of its programme to fill the airline's seats. We would consider the operator's past success in selling its budgeted programme at a profit, and in the light of that whether the new proposed programme seemed attainable.

Where an applicant was not attached to a tour operator, or was attached but intended to make a material amount of revenue from third party sales, we would consider its ability to sell the aircraft in its own right. This would take the form of assessing whether the anticipated daily utilisation per aircraft, load factors and seat rates could be reasonably achieved, making comparisons against existing operators.

2.3 Costs

In considering costs the CAA uses two different methods. For DOCs, one method is to compare the applicant's DOCs per block hour with existing carriers using the same aircraft type and flying as similar an operating pattern as possible. The other approach is to consider evidence on each item of cost separately. For example, aircraft lease costs can be verified by obtaining a copy of the lease agreement. Fuel costs could be verified with reference to manufacturer's data or other independent sources. Airport charges could be verified with calculations deriving from the published schedule of airport charges. If a discount is available to new services, then a letter from the airport confirming this would be sufficient evidence. Handling charges can be verified with a copy of the agreement with the handling agent.

2.4 Re-forecast

Having analysed the plan, it is possible the CAA will regard some of the conclusions as optimistic. Where that is so then we shall wish to re-forecast the plan, based on assumptions which we regard as more realistic. In order to be able to do this, it is useful to have access to a spreadsheet version of the business plan, preferably compatible with Microsoft Excel.

3. CAA VIEW ON FUNDS AVAILABLE TO BUSINESS

In considering whether the proposed level of funding is adequate the CAA analyses the applicant's balance sheet at the start of operations and considers whether it is strong enough in the light of the CAA's analysis of the business plan. The CAA generally considers two aspects of the balance sheet: firstly the concept of free assets, and secondly unrestricted cash balances. The following paragraphs will define these two aspects of funding, and the way in which the concepts are applied will be described in Section 4.

3.1 Cash

Cash is relatively straightforward. The CAA takes the balance sheet definition and then the only distinction is between restricted and unrestricted cash. For example if a bank had a charge over part of the firm's cash, or required a minimum balance to be maintained, then the CAA would not count that as cash in applying the test described in Section 4.1.1.

3.2 Free Assets

A company's free asset position is a modified version of its net asset position, as recorded on the balance sheet. Whereas net assets is the sum of all the company's assets, minus short and long term liabilities, free assets is reached by deducting particular categories of asset from the net assets, and adding back particular categories of liability. Certain off-balance sheet items may also need to be added or deducted.

The mechanics of the calculation are similar to calculation of a company's break-up value. However the additions and deductions made to reach the free asset value are different, and the concepts should not be confused. The underlying principle behind the free asset figure is that it should represent the funds that would be available to support the business throughout the period in question.

For start-up carriers, the calculation is likely to be relatively simple. The following description of the categories of addition and deduction includes categories which are more relevant to an existing carrier than a start-up, and it may be useful to retain it for future reference.

The following notes outline the additions and deductions that are made; they are not comprehensive but will illustrate the principles. The CAA's Finance Section staff will be happy to offer guidance where necessary.

3.2.1 Assets

As a general rule, fixed assets are deducted if they could not be used to support borrowing or sold quickly without harming the business. For example, aircraft are usually allowable at book value (unless the book value seems to overstate the amount of borrowing that the aircraft could realistically support), and the same applies to freehold and long leasehold property (that is, with over 10 years unexpired). Computers, motor cars, short leasehold property and other minor fixed assets would be deducted. In respect of freehold properties held overseas allowance will only be given if a UK branch of an overseas bank confirms the extent to which the asset can support borrowing.

Current assets are deducted unless they have intrinsic worth in the short run, even in circumstances where a company was perceived to be in trouble. The following table shows the treatment of the most common categories of current asset.

Allowed Yes	Notes There is a presumption that this can be used to support
No Yes No	borrowing. Usually misc minor items which would not support borrowing There is a presumption that the debt will be paid Except with independent evidence of recoverability.
Some	Some, such as for insurance, are partly recoverable. Others,
No	such as for brochures or advertising, would have no value if the company was to cease trading and would be deducted. These are rarely recoverable
Yes No	For example, where a bank has taken a charge over cash held by the company
	Yes No Yes No Some No Yes

3.2.2 Liabilities

Short term liabilities are almost never added back, since there is a presumption that they must be paid.

Long term loans can be added back only if the borrower and lender are willing to sign a legal undertaking to the effect that the loan will not be repaid without the prior consent of the CAA. The CAA uses a standard form of words for undertakings formally subordinating the amount, which can be provided on request.

A deferred tax reserve cannot be added back unless it can be demonstrated clearly that, taking reasonable assumptions, there is no prospect of the liability crystallising in the foreseeable future, whether the company continues to trade or not.

Maintenance reserves cannot be added back, since it must be assumed that they reflect a genuine need to keep funds aside to maintain the aircraft, and without which the aircraft would become inoperable. In the event of failure a lessor would normally expect aircraft to be returned with full maintenance undertaken.

The above are all examples of liabilities which have already been deducted to reach the <u>net</u> asset figure. Within the categories of liability which have not been so deducted (the shareholders' funds) there is one further possible adjustment. Where Preference Shares are redeemable, they will be treated as a potential liability and therefore deducted, unless the company signs an undertaking that the shares will not be redeemed without the CAA's prior consent. The standard wording can be provided on request.

The following table shows a sample balance sheet together with the appropriate adjustments.

	£ million	£ million
Balance sheet		
Fixed assets:		
Aircraft	5.0	
Short leasehold building	0.5	0.5
Computer equipment	1.0	6.5
Current assets: Cash	0.6	
Trade debtors	0.6 2.0	
Aircraft security deposits	2.0 1.2	
Current liabilities:	1.2	
Trade creditors	(2.6)	
Other creditors	(1.0)	
Net current assets	()	0.2
Long term liabilities:		
Parent company loan		(5.0)
Net assets:		1.7
Ordinary shares	0.4	
Redeemable preference shares	1.0	
Profit and loss account	0.3	
Shareholders funds		1.7
Free asset calculation		
Net assets shown on balance sheet		1.7
Deductions:		
Short leasehold building	(0.5)	
Computer equipment	(1.0)	
Aircraft security deposits Preference shares	(1.2)	
Total deductions	(1.0)	(3.7)
Free assets		
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The firm in this example has a free asset deficit. The situation would be improved if it and the lenders signed undertakings for either the parent company loan (which could then be added back) or the preference shares (which would then not need to be deducted).

4. TESTS IN ARTICLE 5, PARAGRAPH 1 OF EC REGULATION 2407/92

This paragraph contains the financial tests that the applicant must meet. Although both must be met, the tests are <u>separate</u>; that is to say that each will indicate a particular level of funding, and the higher will apply. If 5.1(a) would be met by initial funding of £4 million, and 5.1(b) would be met by funding of £6 million then the final requirement would be for £6 million, since that would also cause 5.1(a) to be met.

4.1 Article 5.1(a)

The test is that the applicant "can meet at any time its actual and potential obligations, established under reasonable assumptions, for a period of 24 months from the start of operations". The following paragraphs describe the approach that the CAA adopts with regard to the main categories of applicant that it receives.

4.1.1 Airlines

In considering this test for an airline the CAA uses the applicant's business plan, modified by new assumptions that the CAA may incorporate as described above, to project the free asset and free cash position forward on a monthly basis for 24 months. Typically, the CAA will set the level of initial funding to ensure that at their lowest point, neither of these indicators falls below a certain minimum. It should be noted that the CAA invariably seeks a margin of comfort on the free asset low point; it is not enough for the position merely to stay positive. It is not possible to give specific guidance on how this margin is set; the factors that will influence it include the scale of the operation and its inherent riskiness, residual uncertainties in the forecasts, and the possibility of unforeseen events such as fuel price increases and aircraft technical problems.

In some cases the applicant's proposed level of funding may not be high enough, and the projections will indicate that the CAA's minimum is breached. In such cases the CAA would seek enough extra funding to ensure that the minimum is met. To take a simple example: based on proposed funding say of £10 million, the CAA's modified business plan produces a free asset low point of £0.5 million, whereas the required margin of safety is £2 million. The CAA would require extra funding to be enough to make up the difference; that is, £1.5 million making total funding of £11.5 million.

Similar considerations apply to cash, in that the CAA would normally seek a margin of comfort. Under exceptional circumstances an application that was based on overdraft finance might be acceptable to cover a short term deficit, but only where a bank was proven to be irrevocably committed to making the facility available. The facility could not be repayable on demand or subject to unacceptable covenants. In those circumstances of course the facility would need to be larger than the projected requirement, by a margin of safety as described above.

4.1.2 Quasi-Airlines

Some companies wishing to start an airline apply initially for an ATOL, with the intention that the operation of the aircraft will be conducted by an existing Operating Licence holder under a management contract. We refer to such operations as quasi-airlines. Generally speaking these operations are intended to be short term, and already a number of companies which operated as quasi-airlines for a period have been granted Operating Licences.

In considering the financial aspects of the ATOL application, the CAA takes full account of the fact that the costs and risks faced by the venture are that of an airline rather than a tour operator. The standard financial test applied to tour operators, which is suitable for the pattern of the tour operating business, is not appropriate for quasi-airline applicants and the CAA instead adopts, as far as possible, the approach taken towards Operating Licence applicants. Consequently, for the most part the information included in this paper will apply unchanged to such applications. However, there are a number of extra factors that must be considered:

- a) The need for the company to post a bond. As with ordinary ATOL holders the bond is there to provide refunds for passengers if the venture fails. The main impact on the venture is the need either to set aside enough security to guarantee a bank bond (which weakens the balance sheet) or to pay an insurance premium. The bond would normally be based on 15% of forecast turnover, and possibly for significantly more if the company Directors did not sign a personal guarantee to make good any shortfall in the bond if the company conducts more trade than is authorised by its licence. Operating licence holders do not need to make such provisions.
- b) ATOLs are valid for a maximum of one year, and at the end of the licence period the venture would need to apply for the licence's renewal, whereas Operating Licences remain valid unless the CAA revokes them.

- c) When the company decides to apply for an Operating Licence, part of its funding will be the retained earnings (or loss) on its balance sheet. In order to verify this figure, the CAA will need recent audited financial statements. If the applicant's financial year end does not fall at a convenient time, so that the audited statements become available when the Operating Licence is to be granted, it may be necessary for the applicant to organise an extra audit.
- d) In considering the application for an Operating Licence, the CAA must apply the tests in Article 5.1, which are for the initial grant of an Operating Licence. In this case, of course, the quasi-airline will have been operating for some time already and the need to meet 3 months costs while taking no account of income may seem onerous when the routes are already established. However the legislation allows the CAA no discretion in whether to apply the test; as a condition of grant of an Operating Licence the applicant will have to have sufficient funds to pass the test.

Some of the above factors may tend to disadvantage quasi-airlines and this may offset the advantage in being able to commence operations before undergoing the costly and time-consuming process of obtaining an AOC.

4.1.3 Integrated Groups

The CAA periodically receives applications for Operating Licences from existing ATOL holders which wish to start an in-house airline. Whereas the ATOL holder is used to undergoing the financial checks imposed annually by the CAA, the involvement of aircraft will change the nature of the financial checks substantially, not only on application but also each year for the renewal of the ATOL.

As discussed in Appendix A, the group will be reviewed on the basis of its consolidated financial position and prospects; it is not generally acceptable to consider the finances of the airline in isolation.

Whereas the financial test applied to ATOL holders is relatively straightforward, comprising solely the requirement for the group to have sufficient free assets to meet the asset ratio test, for an integrated group it is necessary to ensure that the group also has enough free assets for other capital requirements. In considering the test in Article 5.1(a), the CAA considers the need for capital in three main categories, as follows.

The amount of the required **working capital** is determined by the asset/turnover ratio, in the same way as for the usual test for renewal of an ATOL. In addition to this, the group will need extra capital to pay for **start-up costs** such as training incurred after the balance sheet date; the rationale is that since those costs are not incurred in the usual course of business the group needs enough balance sheet strength to fund them in their own right, without eating into the working capital that is needed to keep the regular business going. Finally the CAA may insist on funding to cover **initial losses**, with the same rationale. The business plan will be analysed as described in Section 3, and if the analysis suggests that the group will make losses then it must have enough free assets to cover these as well. This analysis is the main difference between the treatment of pure ATOL holders and integrated groups, since it is forward looking whereas the ATOL test is largely backward-looking.

In performing these calculations, it is important to watch for double counting of costs. For example, if the CAA tests indicate that provision must be made for a first year loss, but start-up costs were also incurred in that year then the full year loss will already be after deducting those costs; they should not be counted twice towards the funding requirement.

There is no difference of principle between the free asset calculation for an integrated group and an ATOL holder. In practice however it will be necessary to take account of particular deductions which were not relevant when the company was just a tour operator, including aircraft security deposits. Also the template used by the CAA (shown on page 6) is different for integrated groups, reflecting the greater importance of the fixed assets on the balance sheet.

For example, an existing ATOL holder wishes to acquire an aircraft to support part of its tour programme. The projected group risk turnover, comprising the tour operating sales and third party sales on the aircraft, comes to £50 million. The plan indicates start-up costs of £0.8 million occurring in the first year of operation. The group has an irregular profit history, and is currently renewed on the basis of a 5% asset turnover ratio.

This example will consider the funding requirement at the start of operations. Of course it would be possible instead to consider the requirement prior to the start, in which case any costs incurred before the start would need to be deducted as well. In this case however the only start-up costs noted are incurred after the operation has started.

The working capital requirement is straightforward at 5% of £50 million. Assuming that in this case the CAA agrees with the estimate of start-up costs, a further £0.8 million will be required. Lastly, the CAA will analyse the business plan to determine whether a loss seems likely. Consider two cases, Case A in which a profit of £1 million seems likely and Case B in which a loss of £1 million is likely. The funding requirement for grant of the Operating Licence in this case would be as follows:

£ million	Case A	Case B
	£1m profit	£1m loss
Working capital	2.5	2.5
Start-up costs	8.0	8.0
Initial losses	0.0	1.0
Remove double counting	0.0	(8.0)
Free asset requirement	3.3	3.5

In either case the group needs £2.5 million to support its normal trading, in line with the CAA's usual policy on tour operators. In Case A no provision is needed for initial losses, but during the course of the year the group will invest money in the airline. Those funds will not be available to support the business and at the start of the year the group will need enough free assets to meet both requirements. In Case B the provision for initial losses is, of course, after taking account of the start-up costs and they do not need to be funded twice.

It should be noted that whereas the expected loss in Case B increases the funding requirement, the expected profit in Case A does not reduce it. This asymmetry is deliberate and reflects the inherent difficulty of predicting results in tour operations.

If the free asset calculation shows a lower free asset position than the requirement then the group will need to make up the shortfall. This could be done by obtaining more funds, or possibly by the rearrangement of existing finances, such as getting a greater proportion of bonds from insurance companies rather than banks.

The preceding discussion has been written on the basis of operations over a single year. In fact, given the wording of Article 5.1(a) it will be necessary to duplicate the process for a second year, having taken full account of the effect of the profit or loss on the balance sheet at the start of the second year.

Following grant of an Operating Licence, the group will have to send group management accounts and other information to the CAA for monitoring purposes. The information requirements are in fact identical to the requirements of an Operating Licence holder, except that they apply to consolidated group information. The group's ATOLs will of course continue to be renewed annually. Those renewals will be based on the detailed examination that has been outlined above.

4.2 Article 5.1 (b)

This tests states that the applicant must be able to "meet its fixed and operational costs incurred from operations according to its business plan and established under realistic assumptions, for a period of three months from the start of operations, without taking into account any income from its operations."

This test is more straightforward, although again the application may differ slightly depending on the nature of the application.

For scheduled airlines, the process is simply to find the costs incurred in the first three months, excluding passenger-related costs such as commissions, and to ensure that the free asset position at the start of operations is at least as great as this amount.

For conventional charter airlines, the CAA would generally exclude direct operating costs as well, on the grounds that if the airline received no income, it would have no reason to fly. Of course the same rationale does not apply to new scheduled airlines, which typically experience very low load factors in the first months of operation but which must operate anyway.

Finance Section CPG CAA 16 November, 2000 Version 2

1. FINANCIAL INFORMATION REQUIRED FOR AN OPERATING LICENCE

The following sections indicate what financial information will be required for the application for an Operating Licence.

1.1 Which companies should be included?

This question arises where the company is part of a group. In such cases, the CAA is likely to consider the finances of the group as a whole rather than just the company that will hold the Operating Licence. The level at which the CAA considers the finances is referred to as the basis of licensing.

To take the simplest case first, an application may be based on a single company, which is directly owned by investors rather than another company. In that case the CAA would consider the balance sheet and business plan of the company only.

The approach would be more complex if the applicant company was part of a group. For example, integrated groups are usually structured as holding companies which own both airline and tour operating companies. Some airlines are part of a group in which the head company also owns maintenance or perhaps leasing companies.

In these cases, the basis of licensing will typically be the consolidated financial position of the group, which is to say that the CAA would consider the application on the basis of the consolidated balance sheet and consolidated financial projections. Projections would also be needed for each of the individual companies separately, since they would need to be analysed separately. Furthermore, as a condition of grant of a licence the CAA would require a guarantee from the head company that it would honour the obligations of each licence holder. A copy of the standard wording is available from Finance Section on request.

1.2 Balance Sheets and Funding

For all companies (or groups), a projected balance sheet as at the start date of the proposed operation, which includes the effect of any funding that will be injected into the venture should the application be successful, together with:

- a) For a company which has been trading for some time already, the most recent set of audited accounts and a reconciliation with the projected balance sheet.
- b) For a company which has not yet traded, details of any transactions such as start-up costs taking place prior to the projected balance sheet date.
- c) The balance sheet should be accompanied by a breakdown of other debtors and prepayments and stock should be split between rotables and consumables.

Details as to the source of finance and (proposed) shareholders, including their nationality and full details of shares held. Useful supporting documentation would include any shareholders agreements and the articles of association.

Details of any financing agreements in which the company is or expects to be involved, such as overdraft or bonding facilities and aircraft leases. Useful supporting documentation would include the relevant agreements.

Projected monthly balance sheets, for two years from the start of operations again accompanied by the information shown at c) above.

1.3 Profit and loss projections

A detailed trading budget for the company's total operations, starting from the start date of the proposed operation. The projections should be monthly, covering the period prior to start-up and then for a two year period. Full details of the assumptions used in respect of revenue and costs (on a hourly, sector or passenger basis as applicable) should be provided. If discounts are to be provided against published costs at airports, written confirmation will be required from the relevant airport.

For a scheduled operation, the direct costs and revenues should also be broken down by route, and a timetable and fare structure should be provided.

For a charter operation, the projections should show the expected hourly utilisation of the aircraft and the hourly rate.

While the exact breakdown of costs, revenues, and other indicators will vary according to the nature of the operation, the projections should be to a level of detail similar to the templates provided at Appendix B.

1.4 Cash flow projections

A detailed cash flow projection budget for the company's total operations, starting from the start date of the proposed operation. The projections should be monthly, covering the period prior to start-up and then for a two year period. There are a variety of legitimate ways to present cash information, although this should contain similar detail to the template provided at Appendix B,.

A statement of assumptions on the timing of payments.

1.5 Other

Details of the proposed fleet of aircraft and the basis on which they are funded; for example if they will be owned outright then the cost, whereas if they are leased then details of the lease payments and any deposits. Useful supporting documentation would include lease agreements.

It will make the CAA's analytical work faster if the financial projections and balance sheets indicated above can be provided as a Microsoft Excel-compatible spreadsheet on floppy disc, as well as in hard copy.

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Version 2

1. ILLUSTRATIVE FORMAT FOR FINANCIAL PROJECTIONS

The following tables indicate the level of detail that the business plan should include.

A. Profit and loss route information. One table per route.

Month 1 2 3 4 5 6 7 8 9 10 11 12 Annual total

Statistics Flight hours

Block hours Sectors Capacity Load factor Passengers Gross yield Net yield Aircraft type

Revenues Gross passenger

Commissions Net passenger

Charter Bar, duty free Freight Other

Total

Direct Fuel, oil

Operating Eurocontrol/navigation costs Landing fees

Handling
Passenger taxes
Catering
Line maintenance

Line maintenance Engineering

Contribution

In some cases, airlines also produce allocations of some fixed costs on a route-by-route basis.

B. Profit and loss account. A consolidation of the above information plus similar headings to the following table:

Month 1 2 3 4 5 6 7 8 9 11 12 Annual

Fixed operating costs/ Crew salaries overheads Aircraft leases

Aircraft depreciation
Aircraft insurance
Start-up costs

Office salaries Administration Rent/rates Utilities Advertising

Other (specify major categories)

Profit/(loss) before Interest

Interest

Profit/(loss) before tax

Tax

Profit /(loss) before dividend

Dividend

Retained profit

Cashflow forecast. C.

1 2 3 4 5 6 7 8 9 10 11 12 Month Annual total

<u>Income</u>

Gross passenger Commissions Net passenger

Charter Bar, duty free Freight Other

Profit on sale of fixed assets

Share capital Loan capital

Total Income

Costs Fuel, oil

Eurocontrol/navigation Landing fees

Handling
Passenger taxes
Catering
Engineering

Salaries

Aircraft leases

Aircraft insurance

Rent/rates

Utilities

Advertising

Other (specify major categories)

Tax

Dividends

VAT

Other costs Introduction costs

Capital expenditure (detail)

Loan repayments

Deposits

Net bank interest receivable/ (payable)

Total costs

Movement

Opening balance

Closing balance