10.4 GOVERNANCE ISSUES IN AIRPORT DEVELOPMENT: LEARNINGS FROM COCHIN INTERNATIONAL AIRPORT LTD.

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Air traffic to Kerala (described by the National Geographic Traveler in October 1999 as one of the 50 must see destinations and later in April 2001 as the most beautiful place in India) came from tourism and expatriate Keralites and their families, mainly from the Gulf region. It was estimated that more than two million people of Kerala origin were working abroad for whom air was the most common mode (rather, the only available) of travel. Kerala had three functional international airports within 600 km—Trivandrum (Thiruvanantha-puram), Cochin (Kochi) and Calicut (Kozhikode).

The Indian Navy owned airport located in Willingdon Island in the centre of Kochi city had the distinction of integrating multiple forms of transportation (air, sea, rail and road) in a small island. The island also headquartered the Western Command of the Indian navy. The Airports Authority of India (AAI)[20] maintained a civilian enclave in the naval airport. The airport was profitable even though the Indian navy received a substantial share of the revenue generated. The effective runway available for landing was 5000 feet out of a total runway length of 6000 feet which allowed landing of smaller Boeing 737 aircraft with a load penalty (limited passengers and fuel). Strategically Indian Airlines had decided to phase out the 737 series on account of higher fuel consumption and substitute it by larger, new generation aircraft like Airbus 320 and 300. The runway of Kochi airport was not equipped to handle larger aircraft.

The airport had the threat of closure hanging over it. This, along with the need for more direct air connections and seating capacity, generated public opinion towards upgradation of airport facilities. The conservative estimate of expanding the existing runway was Rs 70–72 crores (1991 price levels). There were technical and social issues like the giant crane of Kochi shipyard located close to the aircraft approach path, reclamation of land from the backwater, relocation of the railway line and rehabilitation of 200 households. All these were expected to increase the project cost. The owner of Willingdon Island, Cochin Port Trust Ltd. had reservations about airport expansion. In their opinion, the scope for port expansion would be reduced if land was given for expanding the airport. The Indian navy was also not interested in making investments for developing the airport.

THE COCHIN INTERNATIONAL AIRPORT LIMITED (CIAL) EXPERIENCE

Initial Financing Plan

The fund requirement for a new airport was estimated at roughly Rs 200 crore based on discussions with AAI and aviation experts. One of the subcollectors proposed the idea of raising money from the Gulf based NRIs (Keralites) who stood to benefit most from the new airport. (The Gulf bound air passengers were forced to spend two days in transit in Mumbai or other cities. Their representatives had been demanding direct connections from Kerala. Thiruvananthapuram and Kozhikode airports had direct Gulf connection, but the demand far outstripped supply). Investment could come in the form of interest free loans and donations from NRIs as well as corporates and other societies. Kissan Vikas Patrikas (KVP: a savings scheme of Government of India, which doubled the principal in 66 months) could back the loans. For every Rs 5000, KVP of Rs 2500 would take care of repayment, yielding Rs 2500 directly as cash. GOI had a scheme of lending back 75 per cent of the collected amount to the state government for developmental purposes as low interest, long term loan. Remaining amount could be raised as donations from corporate bodies. Four lakh investors, constituting 20 per cent of Gulf based Keralites could build the airport by contributing Rs 5000 each. (Table 10.4.1 gives details of the initial financing plan).

[20] Airports Authority of India (AAI) was formed by the merger of International Airports Authority of India and National Airports Authority through Airports Authority Act (N0. 55 of 1994). It came into existence on 1 April 1995. AAI manages all airports which handle commercial air traffic. The airports are classified as international and domestic. Domestic is further classified into three categories. AAI also provides air traffic services over the entire Indian airspace and adjoining oceanic areas.

International Airports: This status is accorded by GOI. These airports are available for scheduled international operations by Indian and foreign carriers.

Domestic Airports:

a. *Customs Airports with Limited International Operations:* These have custom and immigration facilities for limited international operations by national carriers and for foreign tourist and cargo charter flights.

b. *Civil Enclaves in Defence Airports:* These are civil enclaves in defence airfields, where limited commercial operations by domestic airlines are permitted. These airports are under the operational control of the defence and AAI uses the facilities on payment basis.

c. *Other Domestic Airports:* All other airports, where domestic airlines are allowed are covered in this category.

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This loan from GOI came at very low interest and long repayment period. Repayment could be made when income from the airport accrued and from the sale of excess land (By design, extra land had to be acquired, keeping repayment in view). The contributors would have privileges like special check in counters, waiting lounge, reserved car parking, directorship in the airport board etc.

Table 10.4.1
Initial Financing Plan (1992)

Categories	in Rs crores
A. Interest Free Deposit from 4 lakh NRI's @ Rs 5000 per NRI	200
B. Money invested in KVP's of Rs 2500 each for repayment in six years when the amount doubles	100
C. Cash in hand (A – B)	100
D. Loan against KVP's (75 per cent of Rs 100 crores)*	75
E. Donations	25
Total C + D + E	200

* GOI loans upto 75 per cent of the money collected, back to the states at very low interest and long repayment period. The money needs to be used for developmental purposes.
Source: CIAL Records.

The new financing plan was submitted to the chief minister (CM) of Kerala by the district collector. Impressed by the innovative fund raising technique (which had no financial burden on the state government) the CM asked the district collector to prepare a proper project report and agreed to the suggestion of forming a charitable society for the purpose of raising money. Meanwhile media carried news about the developments on the airport project which mostly evoked positive responses. The NRI community was particularly enthused by the project. The first contribution came to the district collector as a personal cheque for Rs 20000 from Mr. Jose Maliakal, an NRI from Gulf.

The Kochi International Airport Society

Kochi International Airport Society (KIAS) was incorporated as a charitable society in July 1993. The district collector was appointed the special officer for the airport project and was relieved of field responsibilities.

Despite the limited euphoria about the airport project created by advertising in the local media the funds did not flow in as expected. Abroad, particularly in the Gulf countries, KIAS had to compete with the fund raising attempts of Kozhikode airport. (Kozhikode airport had also adopted the same model for funding on the suggestion from AAI). The scheme could raise only Rs 4 crores, as against the anticipated Rs 200 crores. Mr. C. V. Jacob, a businessman from Kochi made the first contribution of Rs 25 lakhs.

Table 10.4.2
Project Cost (as on 31 December 2000)

	in Rs crores
Land Acquisition and Rehabilitation Expenses	70
Construction Cost—Runway, Terminal Buildings and Other Utilities	160
Interest Capitalized	53
Total	283

Source: CIAL Records.

Formation of CIAL

Meanwhile the land acquisition proceedings had progressed to the stage of issuing notifications under the Land Acquisition Act 1894. (Notification for acquiring about 500 acres for public purpose had been issued by then[21]). It was impossible to revert back. Government of Kerala (GOK) was reluctant to contribute money for the airport at the early stage of land acquisition. To mobilize funds it was decided to incorporate a public limited company. The project was to be funded by equity share capital of Rs 70 crores and loan funds of Rs 130 crores. Thus the CIAL was incorporated on 30 March 1994 as a public limited company with Rs 90 crores authorized capital. KIAS entrusted the responsibility of constructing the airport to CIAL and the special officer was appointed the Managing Director of the company. The existing donors were given the option to convert their loans into equity shares. The project was to be completed in three years and the tentative date for inauguration was fixed as 15 August 1997.

The estimate provided by a British company for building the airport was Rs 500 crores excluding land price. Meanwhile, the Federal Bank Ltd, a scheduled commercial bank that had its origins in the neighbourhood of Nedumbasserry sanctioned a bridge loan of Rs 10 crores for six months, at 15 per cent interest. The bank was convinced to associate itself with the project based on emotional ties with the locality.

Land Acquisition

Three associations of landowners whose land would be acquired were formed. Protests soon began. Demands for stopping the project were made by sections of the people. Some were willing to give up their land, but for a good price. The elected representatives like MLAs had diverse political affiliations. Meanwhile the CM who supported the

[21] The Land Acquisition Act 1894 governed land acquisition by the government in Indian territory. Under the act both central and state governments hold the power to declare land as being required for public purpose and the respective state machinery initiates the acquisition proceedings.

project initially, had to move out of power following an internal political reorganization.

CIAL finally acquired 1300 of the 1400 acres of land it intended. The land acquired for the approach road was more than what was required for a four-lane road. CIAL had plans to commercially exploit the additional land at a later stage. As the land value along the approach road appreciated the original landowners demanded that the excess land be returned. (Their demand had political support and CIAL board had eventually taken a decision to return the land). The original landowners were willing to pay back the price paid during acquisition. However, under the Land Acquisition Act it was near to impossible to work out the return of land which would open altogether another speculative dimension in the already troubled subject of land acquisition.

Close to 5000 trees were cut and spot payment of compensation was made. Since the land was on the approach path of flights, the landowners were prohibited from planting trees in this land even though this strip of land was fertile. Paddy cultivation was not economical. The affected group of landowners had initiated collective action, both legal and political to force CIAL to acquire the land at the same rates which CIAL had paid for the adjoining land.

Land Compensation

The airport authorities used a new option of negotiating with landowners to determine the compensation package. Through negotiation it was possible to build in contentious variables like quality of land, earning potential of the land etc[22]. A broad framework for compensating and rehabilitating the affected people was arrived at after consultations with representatives of the landowner's associations and representatives of political parties. All the negotiations were based on the tactical understanding developed with the opinion leaders. A high power committee chaired by a state minister negotiated the prices with representatives of land owners. CIAL made price offers of Rs 4,000–6,500 per cent (a hundredth of an acre) of dry land and Rs 300–1,800 per cent of wet land (including paddy fields). Provisions of the Land Acquisition Act were to be invoked in case of those who refused the negotiated agreement.

Around 400 court cases were filed and one of them was decided by the supreme court. The land for airport was acquired from about 2,300 landowners. Eight hundred and seventy two households had to be shifted. Those who lost houses were rehabilitated in three locations which came to be called as Six Cent Colonies (since six cents of land was given to each family losing their house). One member from each family which lost both house and land would be considered for direct employment or provided indirect employment opportunities in the airport like taxi permit, managing public telephone facility or vending beverages. As on 28 February 2001, 85 evictees had direct employment in CIAL and 691 were given indirect opportunities.

The hurdles in land acquisition continued at every stage. Runway and terminal building construction could not start as planned because some residents refused to move out. There were some false claims of houses in the form of temporary hutments that came up overnight. They were bargaining for a better deal and creating discontent among those who had willingly given up their property rights. These claims were surpassed with caveats from court and at times through forceful eviction.

In addition CIAL had to deal with socially sensitive issues like relocating three temples, two churches, a burial ground and a mystery tree which had acquired the status of a pilgrimage centre. (The tree located near the proposed runway was considered impossible to fell since it possessed divine powers. However it fell down on a cyclonic night). CIAL followed a liberal approach to relocate the places of worship after detailed discussions with religious leaders, priests and community leaders. All expenses for relocation including cost of conducting religious rituals related to relocation were borne by CIAL.

Building the Airport

AAI had agreed to provide technical advice and runway design to CIAL free of charge. The foundation stone for CIAL was laid on 21 August 1994. CIAL appointed KITCO, a state government enterprise as technical consultants. KITCO was responsible for monitoring the progress of the project and coordination. Absence of clear guidelines and interdepartmental conflicts had almost brought work to a standstill. CIAL could also claim the distinction of not losing even one day of project time due to labour unrest, otherwise a common feature in Kerala.

Financial Resource Mobilization

In March 1995, HUDCO sanctioned a term loan of Rs 25 crores at 16.5 per cent interest. GOK sanctioned Rs 1 crore towards equity. The government contributed the next instalment of Rs 5 crores to equity. Private placement efforts brought in Rs 15 crores as equity.

The company decided to adopt the public issue route. The public issue was discussed with merchant bankers and financial institutions whose response was not very encouraging. GOK indicated its inability to contribute more

[22] The Land Acquisition Act provides two routes to arrive at compensation. The district collector could decide on the compensation or the court upon a reference could decide the same. In the former case there are no concrete guidelines. In the case of court reference there are certain guidelines to arrive at the compensation. The landowners are allowed to challenge the award in the higher court.

resources but was at the same time concerned about losing control if another strategic partner was brought in. The 12th meeting of the board of directors of CIAL suggested that, for maintaining control GOK should hold at least 51 per cent of the equity. The government accepted this decision and a notification was issued in September 1997 in principle enhancing the equity participation of GOK to 51 per cent. This notification became the policy governing future investment decisions in CIAL.

Since GOK was not in a position to contribute its equity share efforts were made in the direction of raising equity from the other stakeholders. Three public sector oil companies were approached for giving refuelling rights in CIAL. BPCL won the exclusive rights in exchange for Rs 5 crores contribution towards equity. Equity contribution also came from other service providers and public. The equity holding community was spread in 30 countries. Majority of the NRI as well as domestic investors were attracted to the project through word of mouth and news about CIAL. The company also contributed its bit towards public relations through press releases and public meetings in different parts of Kerala. NRIs, businesspersons and local self-governments were personally contacted and requested to commit to the project. The idea of owning a share in an airport was emotionally irresistible to many. The public relations drive directly handled by the MD prompted many service providers as well as small investors to look at CIAL favourably.

First Year of Operations

The airport was inaugurated by the President of India on 25 May 1999. Commercial operations started from June 1999 with Air India operating the first flight to the Gulf. Shortly afterwards the commercial enclave in the old airport was closed and domestic operations shifted to CIAL.

The airport had put in place a spacious car park, visitor's gallery, a pre-paid taxi system run through a co-operative society and airport security managed by the Kerala Police. Other airport services like fuelling facilities, public canteen, foreign exchange counters etc. were in place by agencies who participated in financing the airport. Even though GOI had not yet declared CIAL as an international airport (implying foreign airlines could not use the airport) national carriers would operate international flights. Central agencies like customs and immigration required for handling international travellers had been organized. The airport project envisaged handling 17 flights a day during the first year of operations moving up to 31 flights a day in the fifth year of operations.

AAI was the designated agency under the Airports Authority Act responsible for providing Air Traffic Control (ATC) services over Indian airspace. AAI owned airports and all equipments required for ATC was installed by AAI. The facility was managed by a special cadre of Air Traffic Controllers who were AAI employees. According to international convention all airlines travelling through the airspace had to pay for the navigation support provided by ATC. This was a major source of aeronautical revenue for AAI. (The proposed new policy on civil aviation which permitted private participation in airports, had clarified that ATC was AAI's responsibility. However the policy was vague on the investment for ATC equipments and facilities and the revenue sharing between AAI and the private airport. Pending resolution of this issue the inauguration of the airport was impossible.) AAI insisted that CIAL install the ATC equipment while they would manage the facilities and keep the revenue.

The MD of CIAL keeping the date of inauguration in view, signed an MOU with AAI, where all equipment would be installed by AAI for which CIAL would make payments later on a cost plus basis. ATC charges had two components: Route Navigation Facility Charge (RNFC) and Terminal Navigation and Landing Charge (TNLC). According to the MOU, CIAL would reimburse the cost of navigation equipment installed by AAI and allow it to keep the RNFC. CIAL would receive revenue from TNLC levied on airlines. This MOU was subject to the approval of the CIAL board. AAI went ahead and installed the necessary equipments for traffic control.

AAI was the licensing authority for all airports in India. AAI which itself was responsible for constructing and managing the airports gave a permanent license to the airports. Periodic inspections were conducted to ensure compliance to standards. CIAL being the first airport outside the control of AAI was given a temporary license valid for three months. The license was renewable every three months based on regular inspections. CIAL's demand for a permanent license was not accepted.

The closing of the old naval airport to civilian traffic was a precondition for the viability of CIAL. The Indian navy had already recorded its objections about the active civilian enclave on grounds of internal security. However some prominent citizens of Kochi objected to the closure of the old airport and filed a public interest litigation or a PIL. AAI employees stationed at the old airport and the private airline company which had made investments there also acted as pressure groups against shifting domestic operations. There was also pressure from domestic travellers to keep the old terminal open and leave CIAL to handle international flights only. However the court decision and the civil aviation ministry favoured CIAL for domestic operations. The civil enclave in the old airport was closed and the AAI employees were redeployed.

The civilian enclave supported a number of taxis that provided the last leg of connectivity to the passengers. The taxi operators from the old airport had approached the CIAL management demanding rights to operate taxi services. However by that time CIAL had formed a society of evicted people to operate the taxi services. The evictees had approached banks for loans. The initial traffic was not sufficient to provide work for all the taxis. The taxi drivers were under pressure to service the loans. (Some of the taxi owners had borrowed money from private agencies against pledge of the vehicle. The loan disbursement was faster and involved less paper work. Default in payment resulted in the vehicle being confiscated without notice.) Relatives who came with own transport usually received the NRI travellers. Business passengers and tourists used the pickup service provided by the city hotels. The traffic flow in international and domestic terminals were different. The CIAL taxi drivers went to the extent of preventing city hotels from picking up passengers directly from the airport and forced NRIs to use their services. The matter was resolved by re-engineering the prepaid taxi system. In addition restrictions were set for other private vehicles and auto-rickshaws for picking passengers from the terminals. The old airport taxis were disallowed the right to operate from CIAL. Informally CIAL did not press for operating long distance state transport buses from the airport even though such an arrangement could have benefited the passengers. In return the taxi drivers had voluntarily agreed to follow a CIAL managed allocation and payment system. They also agreed to a code of conduct with passengers.

CIAL had decided to allow a single agent to handle the ground service operations in CIAL. This was the common international practice. Air India was given the exclusive rights through open bidding and a high profile pitch made by the Chairman, Air India to the Board of Directors. Other parties involved in the bidding process approached the court against the order. The domestic private airline Jet Airways also approached the court citing that the exclusive agent arrangement that too by a rival airline company was detrimental to customer service.

CIAL had high expectations on revenue generation from cargo operations. The responsibility of managing the cargo operations was entrusted to Air India on a revenue sharing basis. (15 per cent of cargo revenue would accrue to CIAL.) The cargo operations failed to reach expected levels since according to CIAL the tariff rates of AI was high.

At the time of inauguration of the airport the company was already facing the interest burden from loans taken from banks and FIs, particularly HUDCO. This information led to speculations regarding the viability of the airport and even the probable closure of the airport. This had its effect on investor confidence.

Competition from Kozhikode and Thiruvananthapuram could not be discounted. When CIAL started operations Air India and Indian Airlines diverted some of their international flights from these airports. All the three airports required more flights to be viable. In the process, the lobbying done by the state government got diffused and all three airports were competing between themselves to protect their existing flights. Even before the inauguration of the airport, several international airline companies had indicated their willingness to operate direct flights from CIAL which included diverting existing flights from neighbouring states. CIAL was able to obtain virtual monopoly of allowing chartered flights carrying pilgrims for performing Haj ceremony. The airport had anticipated the market and built special facilities for catering to Haj pilgrims. Kozhikode airport was directly competing with CIAL for the Haj flights.

On the land acquisition front CIAL continued to face hurdles. The critical Instrument Landing System (ILS) commissioning was delayed because of the failure to acquire land and remove obstacles (including houses) that fell in the glide path of the aircraft. Lack of ILS was cited as a reason which delayed the international airport status for CIAL and had created discomfort to passengers and airline companies. The delay which came from the GOK side inspite of the fact that all the owners were willing to surrender their land for a negotiated price was attributed to vested interests operating in other airports. In addition, land acquisition proceedings for the approach road and the eastern end of the runway was in progress.

Into the Second Year: At Crossroads

In a strict sense CIAL was not a private airport. GOK through a board level resolution had decided to hold minimum of 51 per cent stake in CIAL. This would be achieved through direct contribution from GOK and investments from profit making state enterprises. Central PSUs like AI and BPCL also held equity stake in the company. In strict sense CIAL could be defined as a joint sector airport with private–public participation. Even as on March 2001 the state government had not contributed its full share of equity capital.

GOI controlled awarding landing rights to airline companies which allowed them to operate from a specific airport. India has so far entered into bilateral air service agreements with 96 countries out of 185 countries that were part of ICAO (International Civil Aviation Organization), out of which 54 involved Air India. According to the civil aviation minister, (Business India, June 11–24, 2001) the demand for bilaterals came from state governments interested in more connectivity for their respective populations. In spite of demands from passengers request from GOK and applications made by various foreign airline companies, no decision was taken until March 2001. In April 2001 the central government allowed one foreign airline to operate from CIAL. Applications from other airline companies were being processed.

Aircraft refuelling was another revenue earning activity that was envisaged and oil companies had created necessary infrastructure, particularly a fuel hydrant system that could reduce refuelling time considerably. CIAL could not exploit this revenue earning facility also. Lack of traffic affected the non-aeronautical revenue stream also since this had a direct relationship with passenger traffic.

Right from the first day of commercial operations CIAL followed the tariff structure adopted by AAI for landing charges since any new tariff structure had to be ratified by AAI. The landing charges were fixed based on the weight of the aircraft. According to CIAL the AAI tariff structure was inappropriate for new airports since the cost structure of AAI airports and CIAL were different. A flexible tariff structure would have enabled the airport to offer innovative and flexible packages to airline companies. In addition CIAL faced difficulty in collecting the charges from PSU airline companies.

On the cargo front customers preferred to take cargo to Thiruvananthapuram or Kozhikode. AI was not proactively marketing their services to exporters. Hence the facilities and capacity created by CIAL were unused. CIAL took over the cargo operations from AI and started to manage the operations with its own staff. Efforts to promote the cargo operations included direct contact with exporters and construction of a cargo village in the airport land modelled after the Dubai cargo village. AI did not take this move very kindly.

The MOU signed between AAI and MD, CIAL regarding ATC payment was rejected by the board of CIAL. According to the MOU, CIAL was to receive revenue only from TNLC levied on airlines. As per CIAL the RNFC receipts were four to five times the TNLC. CIAL refused to honour the MOU commitment since it implied that CIAL had to reimburse AAI to install and maintain the ATC equipment while AAI received the bulk of the revenue. CIAL argued that the revenues already received by AAI from RNFC was sufficient to provide a 60 per cent return on investment or ROI on AAI's investment. This standoff came in the way of upgrading the navigational facilities including installing radar facility (estimated to cost Rs 25 crores). Further CIAL argued that under the AAI Act and the draft policy on aviation, AAI was bound to provide ATC services over Indian airspace. CIAL was ready to allow AAI to keep the entire RNFC revenue if AAI was responsible for investment in ATC equipment and its maintenance. On the other hand it sought a share of RNFC revenue from AAI.

Security services in the airport became a subject of concern for CIAL. Initially the state police had the responsibility for maintaining airport security. The police department charged the airport a fee for the services. Later the services of a professional security agency were enlisted for traffic control, parking area management etc. In view of the increased threat perception to aircrafts and aviation infrastructure, GOI had unilaterally handed over the responsibility of airport security to a paramilitary force, Central Industrial Security Force (CISF). The cost involved in maintaining CISF in an airport was considerably higher than using the services of the state police. The airport had no direct control over CISF since it would be under the Commissioner of Aviation Security, Ministry of Civil Aviation. However the airport had to bear the expenses of CISF and provide required infrastructure like family housing and transportation. Moreover there were concerns about the customer friendliness of an organized paramilitary force. (CISF itself had commissioned a customer perception survey, the results of which indicated otherwise). CIAL was able to negotiate an arrangement with AAI where the expenses for maintaining CISF would be subsidized and the company would forfeit a large share of the passenger service fee component in the flight ticket in favour of AAI.

Revenue Model

The monthly average flights were 280 in the domestic sector and 109 in the international sector during the initial operations until December 2000 while the projected averages were 330 domestic flights and 190 international flights even during the first year. The international flights were less since foreign airlines could not land at CIAL. Even after the declaration as an international airport, lack of bilateral agreements did not allow foreign airline landings in CIAL, in spite of requests from several of them.

The business model of CIAL was heavily dependent on the Gulf based NRIs. Employment trends in the Gulf region indicated that job opportunities were shrinking as a result of the Emiritization drive and fast-changing job profiles in Gulf countries. Unskilled and semi-skilled labourers who had gone during the boom period were returning in thousands causing a severe strain on the Kerala economy. At the same time the trend was shifting towards employment markets in Europe, the Far East and US. Kerala was also fast becoming a tourist destination and a critical point in the southern circuit considered as the alternative to the traditional golden triangle. However the national carriers were restricting themselves to the Gulf sector which was very lucrative for them. Allowing direct flights from other sectors were necessary for long term viability of CIAL. This would pre-empt the competition from Kozhikode which has Gulf bound traffic as the only market segment as well as boost the tourism development efforts of Kerala.

The cargo operations began in September 1999. In the first 16 months until December 2000 the monthly average was 159 tonnes in the domestic sector and 244 tonnes in the international sector, adding to a total of 403 tonnes. The projected average for the first year of operations was a total of 1250 tonnes. It is interesting to note that in the international sector, the export traffic was twice the import traffic.

The monthly average operating expenditure was Rs 62 lakhs during the period June 1999 to March 2000 and Rs 59 lakhs during April to December 2000. During the latter period, the actual was about the same as projected. The personnel costs were restrained to half the projected through control on intake and deferring the revision of compensation structure. (CIAL had patterned the compensation following AAI. When the AAI stakes were revised only AAI deputationists were paid according to revised scales.) While maintenance charges were lower than projected, the general expenses were higher. The expenditure on electricity and water charges as well as reimbursements to AAI were significantly higher than the projected figures.

CIAL had an operating surplus right from the first year of its operations. However the margin was inadequate to cover the debt servicing. As per projections, complete debt servicing was expected to be feasible from the second year. The actuals indicate otherwise leading to the need for financial restructuring.

Corporate Governance

The position of chairperson, Board of Directors CIAL was held by the CM of Kerala. Other members of the board were elected legislators, bureaucrats, FI nominees and investor directors. The board had provision for 15 members including three positions reserved for nominees of financial institutions. The composition of the board as on 31 March 2001 indicated that two positions of FI nominees were vacant.

The composition of the board, particularly its political nature had been a subject of criticism. Apprehensions about political and official influence on the CIAL project were raised at different points of time. However CIAL was of the opinion that the presence of the chief minister and legislators as board members facilitated the company to work around complex governmental systems, particularly land acquisition.

The minority shareholders (Indian public and NRI's) numbering around 10,040 had also demanded representation in the board. Under the umbrella of Cochin International Airport Share Holders Association (CIASHA) their nominees had planned to contest for directorship. However on request of the chairman (CM of Kerala), the nominations were withdrawn. The other demands placed by the association included immediate payment of dividend, while an infrastructure project in normal course required high gestation period.

The general elections conducted in April 2001 witnessed a complete reversal of fortunes of the then ruling front. The new political alignment (which was in power while the project was initiated) had reiterated its commitment to the development of CIAL. However a section among them demanded removal of all political nominees of the previous government from the board of CIAL and that the new CM should assume chairmanship of the board. One argument was, since, the CM of Kerala occupied the position of chairman of CIAL board, the previous CM automatically ceased to occupy the position. However there was another point of view. Since the existing board appointment was made by the annual general body meeting or AGM, it would be prudent to wait till the next AGM for appointing the chairman. In addition a former CM of Kerala also indicated an interest in the chairmanship. Air India which had equity and other financial investment in CIAL also demanded board level representation. They also cited the absence of air transportation professionals who could offer guidance to the company at the board level as a risky practice.

Capital Structure

The project cost as on 31 December 2000 was Rs 283 crores including capitalized interest (Table 10.4.2). Table 10.4.3 gives the capital structure as on 31 March 2001. CIAL had an authorized capital of Rs 90 crores and a paid up capital of Rs 78.93 crores as on 31 March 2001. The government of Kerala. (as per a CIAL Board decision dated 23 September 1996 and the related government order or GO dated 29 August 1997) had decided to hold at least 51 per cent of equity in CIAL directly and through state owned enterprises. This was to have effective government control over the company. The GOK contribution stood at Rs 32.45 crores, which was 39.85 per cent of the paid up capital. To make the GOK share 51 per cent, under the current paid up capital the authorized capital has to increase to Rs 94 crores. GOK would have to bring in Rs 15.5 crores (see Tables 10.4.2–10.4.3).

Airport service providers (Air India, Bharat Petroleum Corporation Limited, State Bank of India and Federal Bank) had brought in Rs 21.25 crores as equity. NRI directors and their relatives contributed Rs 14.14 crores. Six thousand one hundred and sixty Indian residents and 3880 NRIs were equity holders in the project with contribution of Rs 4.48 crores and Rs 5.4 crores respectively. The NRI investors were spread in 30 countries. Two banks—India Overseas Bank and Dhanalskshmi Bank Ltd. together contributed Rs 0.75 crores as equity.

In order to make payments towards HUDCO term loan CIAL wanted to raise additional equity by offering a 1:1 rights issue. The closing date for rights issue had to be extended twice. The GOK's inability to contribute its share had shaken the confidence of other investors who refused

Table 10.4.3
Capital Structure (as on 31 March 2001)

	Rs crore
Equity Participation	
Government of Kerala and Public Sector Undertakings	32.45
Non-Resident Indians and others	24.23
Airport service providers	21.25
Total	77.93
Loan Funds	
HUDCO—Term Loan	152.72
Federal Bank	24.69
State Bank of Travancore	27.51
District Cooperative Bank	12.00
Total	216.92
Interest Free Deposits	
M/s Air India	11.00
M/s. Thomas Cook	0.50
M/s. Indian Oil Corporation	0.75
M/s. Alpha Retail—Duty Free Shop	10.00
Retail outlets	2.75
Total	25.00
Total	319.85

Note: The equity contribution of non resident Indians and others was expected to be Rs 36.3 crores, to make the total equity Rs 90 crores.
Source: CIAL records.

to subscribe unless GOK contributed its full share. Further, the rules disallowing capital and dividend repatriation prevented NRI investors from contributing to the equity. (In April 2001, the foreign investment promotion board or FIPB allowed dividend repatriation). The rights issue which could generate equity up to Rs 188 crores, had failed to raise any money.

During the initial stages CIAL had offered equity stake to the Airport Authority of India. AAI rejected the offer on the grounds that the AAI Act did not permit equity holding. According to press reports while the international investment community and the Indian FIs had shown interest in CIAL the state government was against such investments due to perceived dilution of its interest.

Implications for Governance

Land Acquisition

All matters related to acquisition of land for project purposes were governed by the Land Acquisition Act of 1894. The Act empowered the central and state governments to acquire land for what was considered to be public purpose. From inception, the term public purpose has been defined in vague terms. The Supreme Court also supported the view that the term need not be defined strictly. The apex court was of the view that, the conditions which existed during the time of acquisition need to be taken into consideration and hence it would be better if the term is not clearly defined. The power of the act could be leveraged by the government for notifying the intention of taking the land. The process also gave opportunity for the affected public to voice their reservations. Past experience of land acquisition in India showed that the process led to acquiring more than the required land. The additional land was often kept without any economic activity. The CIAL project also acquired more land than it wanted for its core operations and further expansion. Further, the project had built in income from land sale and commercial exploitation of surplus activity as major sources of revenue.

During the process of land acquisition complete information about the extent of land required was kept hidden from the public. In this case land acquisition and the project proceeded almost together. While this approach could have phased the pressure on payments, operationally it was not a desirable process. At a later stage the project layout had to be altered under political pressure and to meet the convenience of influential individuals. The process that followed led to avoidable misperceptions among public and considerable energy had to be diverted to resolve the conflicts. A section of landowners were able to obtain a decision from CIAL board to have their land returned. This decision which is awaiting governmental approval could set a precedence of returning the land acquired for public purpose.

To clear the flight path, trees in the flight path area were cut and compensated by evoking the relevant provisions of Aircrafts Act. While the land ownership remained there were restrictions on further construction in the area. The residents of the area suffer noise pollution, loss of agricultural income and damage to houses. The application of Aircraft Act denied compensation for any of the above effects. Legal and mass action was initiated to have CIAL acquire the land and compensate. The differences which would arise due to application of the two different acts need to be dealt with.

Compensation for acquired land was a contentious issue in land acquisition deals. The practice for determining the price based on prices declared in governments records would not work. Such prices are normally understated. Acceptable compensation could be arrived at only by leveraging the political process and at rates close to real market value. It was equally important to manage the public perception that the evictees had received a fair deal and the local community would also benefit from the project. In spite of this there would be legal battles that need to be anticipated and prepared for.

Rehabilitation and Resettlement

Land acquisition often resulted in depriving a set of people the livelihood and quality of life they were used to. The process also harmed the fragile cultural fabric which was shared by the community. The mechanical process of compensation payment and resettlement did not always help them to effectively rebuild their lives. Experiences of similar schemes were not very encouraging.

Rehabilitation schemes conducted with proper socio-economic assessment of the locality with emphasis on family and cultural identities, could reduce the pain of relocation. In addition, community participation in the scheme through open dialogue and involvement of political, social and religious leaders who had the trust of community members could ensure speedy resolution of conflicts. Community members also expect their own economic upliftment in return for the sacrifice made. They would invariably support projects which provide them with such opportunities. Involvement in the form of direct employment or indirect benefits was the acceptable convention. Here also legal battles and hard bargaining should be expected and prepared for.

Viability of Airports

It could be observed in the Indian context that decisions about locating airports are at times based on political considerations rather than commercial viability. Kerala's proposed fourth airport to be located at Kannur was gifted by a civil aviation minister who was born in Kannur. This decision was announced in a public meeting, inspite of the fact that there are two functional airports in the vicinity—Kozhikode and Mangalore. Even though traffic studies conducted by AAI indicated that the airport was economically not viable, political interference led to identification of land and even eliciting commitment from private sector investors (including a member of a Middle East ruling family known for making high profile investments). Similar experiences could be traced in other states also.

This raised serious questions about demand assessment, competition policy and governance. In the absence of clear guidelines, governments can encourage pure speculative and political interests affecting the viability of an airport with a significant capital investment.

Risk Mitigation

CIAL faced a variety of risks including political risk, revenue risk, operating risks and regulatory risk.

The political risk was due to non-continuity of political leadership, lack of clarity on the decision making roles of the centre and the state, and local political activism. Effective corporate governance and clear national policy on air infrastructure would be essential to mitigate this risk.

The revenue risk was due to demand uncertainties (driven by the market environment, service and policy on bilateral agreements) and pricing. This risk can be mitigated by creating a better dependence on non-aeronautical revenues, developing and executing marketing strategies aimed at different market segments (foreign and domestic airline companies, charter flight operators, cargo), being customer friendly in service delivery, lobbying for more traffic through bilateral agreements and in doing sufficient homework to take appropriate pricing decisions.

The operating risks were due to cost escalation, unanticipated delivery of obligatory services like security in the manner determined by external agencies, staffing, labour union relations and lack of coordination among various agencies. Each of these causes of risk are complex and need to be dealt with in a generic manner through better anticipation and professional management.

The regulatory risks were due to uncertainty in licensing (by DGCA), tariff fixation and revenue sharing (with AAI). Clarity in the policy for air infrastructure would help mitigate the risk.

Staffing

Key people who managed the airport development came from the state government services and AAI. The first MD was from the IAS with prior experience in district administration and management of state enterprises. CIAL had recruited some senior professionals for critical positions like finance, fire services, company secretary etc. from the market. All technical personnel came from AAI on deputation. Staff for critical administrative functions like personnel and administration, land acquisition etc. came on deputation from state government. Some deputationists chose to join CIAL at a later stage. The state government appointed the present managing director, who also belonged to the IAS. (The present MD had prior experience of managing major infrastructure facility in Kerala, even though by cadre affiliation belonged to another state.)

Airport operation is a niche area that requires high quality trained personnel. Currently AAI is the only source of trained people, which has developed its captive recruitment and human resource development capabilities. As private airports increase the natural inclination will be to recruit personnel from AAI. This might hurt the interests of AAI and eventually lead to strained relationships. (The national air carrier, Indian Airlines Ltd. faced a similar situation when the airline sector was opened.) Planned interventions at the national level to develop human resources for managing airports are required.

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