

Guidance for Financial Analysts to model the impact of aircraft noise on Flughafen Zürich AG's financial statements

Zurich Airport, March 17, 2015

Introduction

The objective of this document is to explain the impact of aircraft noise on the accounts of Flughafen Zürich AG. In the area of formal expropriations, the Swiss Federal Supreme Court rulings on fundamental issues in the first half of 2008 enabled Flughafen Zürich AG to reliably estimate the total cost for formal expropriation compensation for the first time, despite remaining uncertainties regarding the accuracy of this estimate. On the basis of the fundamental issues decided by the Swiss Federal Supreme Court, the noise related costs that were reliably estimable (“base case”) as at June 30, 2008 totaled CHF 759.8 million (including formal expropriations, costs for sound insulation and resident protection and all related operating costs) for “new” and “old” noise-related liabilities.

“New” noise-related liabilities refer to those arising since Flughafen Zürich AG is the holder of the concession of Zurich Airport, i.e. since 2001. The noise-related liabilities arising from previous periods, when the Canton of Zurich was the holder of the concession, are called “old” noise-related liabilities. The Canton of Zurich assumed the pre-financing for these noise-related until November 30, 2014.

With the release of the full year 2010 results (annual report 2010) the expected total noise-related costs were updated as a result of a Swiss Federal Court decision from June 2010 on the foreseeability of east approaches. The total expected most likely noise-related costs could be reduced from CHF 759.8 million to CHF 739.5 million. However, the portion to be borne by Flughafen Zürich AG increased because of a higher share of “new” noise-related liabilities.

The total expected most likely noise-related costs were adjusted again with the release of the full year 2011 results (annual report 2011) in order to reflect a Swiss Federal Court decision from December 2011 on the methodology of how to calculate the indemnifications for reduced value of yield properties. As a result, the total expected most likely noise-related costs were slightly adjusted upwards from CHF 739.5 million to CHF 740.6 million. The portion to be borne by Flughafen Zürich AG increased again to 76%.

As per November 30, 2014 the pre-financing of noise liabilities by the Canton of Zürich became obsolete. Flughafen Zürich AG has assumed the still unpaid “old” noise-related liabilities in the amount of CHF 106.4 million and in return has received back the Canton of Zurich’s corresponding share of the assets from the Airport of Zurich Noise Fund (AZNF) in the amount of CHF 224.2 million (“reversal of pre-financing through the Canton of Zurich” – hereinafter called “**reversal**”).

As per November 30, 2014, the splitting of noise charges is also no longer applicable.

Financial impact of reversal

The reversal increased the assets and liabilities of Flughafen Zurich AG by CHF 106.4 million each:

- Increase of the Airport Zurich Noise Fund (cash and cash equivalents, current assets, non-current financial assets) in the amount of CHF 224.2 million.
- Increase of provision for formal expropriations (current provision, non-current provision) in the amount of CHF 106.4 million.
- Reduction of the intangible asset from right of formal expropriation of CHF 117.9 million.

The reversal itself had no direct impact on the 2014 income statement.

But as a result of the abolishment of the split between “new” and “old” noise-related liabilities, the income statement and the balance sheet of Flughafen Zürich AG will be affected differently going forward.

Regulations of the Airport of Zurich Noise Fund

In addition to this guidance, we also recommend reading the regulations of the Airport of Zurich Noise Fund: www.zurich-airport.com/aznf.

Definitions

Noise-related costs

- Costs for formal expropriation
- Costs for measures regarding sound insulation and resident protection
- Operating costs in regard of aircraft noise

A list of all cost components, split in more detail, is additionally available in the regulations of the Airport of Zurich Noise Fund.

Noise-related charges

- Daytime noise charge as an addition to the landing charge
- Night-time noise charge (for take-offs and landings between 09:00 p.m. and 07:00 a.m.)

The noise-related passenger charge was suspended as per February 1, 2014. Before, CHF 5.- per departing passenger were levied as noise-related passenger charge.

All noise-related charges are fully and explicitly dedicated for noise-related costs. Once the formal expropriation and sound insulation and resident protection payments have been settled completely, the objective is to have a zero balance in the AZNF. Therefore, the level of the noise-related charges will be adjusted accordingly within the existing rules.

Split of revenues

Starting as per December 1, 2014, all noise-related charges are recorded as revenue within the financial statements of Flughafen Zürich AG.

Historical Split:

- Up to June 30, 2008: 100% FZAG
 - After July 1, 2008: 53% FZAG; 47% Canton of Zurich
 - After January 1, 2011, 72% FZAG, 28% Canton of Zurich
 - Between January 1, 2012 and November 30, 2014, 76% FZAG, 24% Canton of Zurich
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Airport of Zurich Noise Fund (AZNF)

The AZNF is a liquidity-based fund that does not take the form of any type of legal entity. The statement of the fund presents the accumulated surplus or shortfall as of balance sheet date arising from noise-related charges, less expenses for formal expropriations, sound insulation and resident protection as well as operating costs.

Impacts of noise-related revenues and costs on the income statement

Noise-related revenues and costs form an integral part of the company's overall financial statements.

- All noise-related revenues and costs are fully recognized within the income statement of Flughafen Zürich AG.
- Income statements of a single year were showing higher revenues than costs until the year 2013. Thus "noise" had a positive impact on net income of Flughafen Zürich AG. Because of the suspension of the noise-related passenger charge as of February 1, 2014, the impact was negative in 2014 and could also be negative going forward. Whilst a single year can be "distorted" as explained above, over the entire period until all noise-related costs are settled, impact on income statement as well as on cash flow will be neutral.

Revenue impact

The noise-related passenger charge has been suspended as per February 1, 2014.

As per May 1, 2013 the model for noise-related landing charges was adopted to ensure the underlying incentive mechanism for less noisy aircrafts. Income from noise-related landing charges will be in a low double digit million amount going forward; higher charges due to more traffic might be offset by reductions due to less noisy aircrafts and lower MTOW's.

Should the noise-related charges change in the future, revenue from noise would change as well.

Operating cost impact

Operating costs are already today and will also in the future be included in various cost items of the P&L such as for example cost of personnel, maintenance or general administration of the noise department. Therefore they do not have to be projected separately.

Historical impact:

- 2008: CHF 4.3 million
- 2009: CHF 4.7 million
- 2010: CHF 4.3 million
- 2011: CHF 4.3 million
- 2012: CHF 3.8 million
- 2013: CHF 3.9 million
- 2014: CHF 3.9 million

The reversal as per November 30, 2014 has no impact on operating costs going forward.

Important: cost for formal expropriation payments and for sound insulation and resident protection are not recorded in the income statement when payment is made, but are reducing the separate provision (see also impact on balance sheet below).

Amortization impact

As a result of having recorded an intangible asset in the balance sheet starting June 30, 2008, FZAG will have to amortize this asset on a straight-line basis until the end of the concession, i.e. until May 2051.

Historical impact:

- 2009: CHF 5.6 million
- 2011: CHF 7.0 million
- 2012: CHF 7.7 million
- 2013: CHF 7.7 million
- 2014: CHF 7.5 million

As a result of the reversal as per November 30, 2014 the amortization impact going forward will be lower (approx. CHF 4.5 million) than in the years before because of the lower intangible asset for formal expropriation.

Financial expenses impact

The unwinding of the discounts of both provisions (provision for sound insulation and resident protection as well as the provision for formal expropriations) happens through the line item financial expenses (non-cash effective). The future amounts for unwinding depends a) on how the cash out for formal expropriation payments and sound insulation and resident protection arises and b) on the level of the discount rate as required by IAS 37.

Historical impact:

- 2008: CHF 5.1 million (cost)
- 2009: CHF 7.8 million (cost)
- 2010: CHF 8.6 million (cost)
- 2011: CHF 13.4 million (cost)
- 2012: CHF 25.8 million (cost)
- 2013: CHF -6.2 million (income)
- 2014: CHF 7.7 million (cost)

The increase in 2012 was mainly driven by a significant reduction of the respective discount rate.

Due to an increase of the discount rate together with a reassessment of the timing of respective cash outflows, an income of CHF 6.2 million resulted in 2013.

Losses on financial assets of Airport Zurich Noise Fund are also included in the financial expenses (2014: CHF 1.7 million).

Financial income impact

Interest income on financial assets of Airport of Zurich Noise Fund is recorded as financial income.

Historical impact:

- 2008: CHF 6.1 million
- 2009: CHF 3.4 million
- 2010: CHF 3.5 million
- 2011: CHF 3.3 million
- 2012: CHF 4.6 million
- 2013: CHF 5.3 million
- 2014: CHF 3.8 million

Gains on financial assets of Airport Zurich Noise Fund are also included in the Financial Income.

Tax impact

The expected income tax rate of Zurich Airport can in principle be applied also for noise-related revenue and cost projections. The note on deferred taxes (refer to page 100 of the Annual Report 2014) shows the exact amount of deferred tax expense as a result of noise.

Impacts of noise-related assets and liabilities on the balance sheet

Assets and liabilities related to noise are included mainly in the following balance sheet line items:

- Current and non-current financial assets (Airport of Zurich Noise Fund)
- Intangible asset from right of formal expropriation
- Provision for sound insulation and resident protection
- Provision for formal expropriation

Intangible asset from right of formal expropriation

The intangible asset from right of formal expropriation will be further amortized on a straight-line basis until the end of the concession, i.e. until 2051. Amortization started on July 1, 2008.

Historical value:

- 2008: CHF 239.0 million
- 2009: CHF 233.3 million
- 2010: CHF 285.5 million
- 2011: CHF 305.4 million
- 2012: CHF 297.7 million
- 2013: CHF 289.9 million
- 2014: CHF 165.9 million

Provision for sound insulation and resident protection & provision for formal expropriation

Payments for sound insulation and resident protection as well as payments for formal expropriation decrease the provision.

According to IFRS, the provisions are recorded at a discounted value and had to be unwound with a discount rate on an annual base. The discount rate has reduced in 2010 to 3.5% (from 4%), in 2011 to 2.5% and in 2012 to 1.2%. In 2013 the discount rate has increased to 1.5% and has reduced again in 2014 to 1.1%

Historical value for provision for sound insulation and resident protection:

- 2008: CHF 118.8 million
- 2009: CHF 115.6 million
- 2010: CHF 110.6 million
- 2011: CHF 100.4 million
- 2012: CHF 86.3 million
- 2013: CHF 65.7 million
- 2014: CHF 46.1 million

Historical value for provision for formal expropriation:

- 2008: CHF 125.8 million
- 2009: CHF 130.8 million
- 2010: CHF 192.3 million
- 2011: CHF 233.3 million
- 2012: CHF 248.1 million
- 2013: CHF 239.7 million
- 2014: CHF 352.3 million

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