Size isn't everything

Len Kirsch proposes additional contract clauses to take into account the uncertainty of the longer term agreement.

Long term contracts.
Sounds great?
Not always.

Long term agreements can be a problem without a mechanism for price increases when unforeseen circumstances inflate the cost of providing those services.

Remember, the IATA SGHA provides for termination on 60 day notice unless Annex B creates an exception by adding a longer or set term. The SGHA ignores the fact that a ground handler may require a term or even a long term agreement in return for investing large amounts of money in ground support equipment and other start-up costs. Otherwise, how does a company spend money, negotiate purchase agreements, sign a lease for a break room, office space and possibly ramp or cargo warehouse space, not knowing if the carrier will continue the contract for an extended period – or if it will cancel after 60 days' notice? Have any of you lost a contract when a competitor makes an unsolicited bid for your contract?

Nothing stops parties from negotiating term agreements, even long term agreements, but the price for a term agreement is usually a set price. But in this day and age, how can any company foresee its costs a few years ahead?

There are several options available to ground handlers, including agreeing to renegotiate if governmental compliance costs grow unexpectedly (something insisted on by US handlers when national health care was first discussed); or where parties could agree to renegotiate if airline frequency changes by more than a certain percentage. A common provision allows negotiations for increases or decreases in prices if flights increase or decrease by more than five percent.

If agreement is not reached, the parties seeking the change in price can terminate the agreement, even if term remains. This works when a carrier's growth is restricted through gate limitations or other restraints on growth. However, with mergers, rationalisation by gate exchange and other unforeseen changes in airline operations, lately no-one has been able to foresee when a carrier will need additional services over and above (or greatly less) than what was negotiated at the time the contract was signed.

While negotiating such provisions seems simple enough, in reality often the carrier and the ground hander are not in an even negotiating position - especially if the ground handler is already handling the carrier and is concerned that losing the airline will create a gap in work for its staff between flights. Rather than leave it to carriers and ground handlers to negotiate changes in contracts in the event of alterations to operations, I am suggesting that carriers and handlers commence discussions about future changes in the SGHA, which can ensure fair and equitable price changes in term agreements based on actual costs, size of operations, governmental impositions and changes in circumstances.

Let's be honest: handling prices are not rocket science. Prices are set by calculating a ground handler's fixed and variable costs, plus a set profit. Neither the airline nor the ground handler benefit when prices are set too low or too high. Accurate pricing ensures that ground handlers have sufficient revenue to ensure that each and every employee is well trained, can utilise all necessary and appropriate safety equipment, that ground support equipment is well maintained and that both carrier and ground handler benefit.

I understand that carriers base their fares on budgets. However, budgets should be based on real costs during the budget period. Even if a carrier benefits from a low price during one budget period, it is likely that it will be at a disadvantage during the following budget period when the ground handler seeks to offset its losses by higher prices. If a ground handler is stuck in a long term contract, won't it have to make up for any prior losses by increasing prices in future contracts?

So how does the industry handle long term contracts yet at the same time allow some flexibility for changed circumstances? What I suggest is the addition of a new standard provision, such as the following.

"In the event that there is an unforeseen material change in flight schedules or in the amount of flights at any airport, or if the Handling Company's expenses increase materially due to unforeseen circumstances, then the Handling Company may request that Carrier negotiate changes in fees in good faith based on objective criteria. If the parties are unable to reach agreement within sixty (60) days of notice seeking negotiation by the Handling Company to the Carrier, the Handling Company may give Carrier sixty (60) days' notice of termination of the Agreement. If, during the notice period, the Carrier agrees to the Handling Company's price increase, the Handling Company shall continue to perform the Services notwithstanding the notice of termination".

Of course there can be other provisions, different wording and other criteria. The key is to find a flexible means of providing for long term contracts, with the possibility of changes in pricing in the event of unforeseen or changed circumstances.

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