MESA AIR GROUP INC
Form 10-K
December 28, 2001

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)

OF SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended September 30, 2001

Commission File Number 0-15495

Mesa Air Group, Inc.

(Exact name of Registrant as specified in its charter)

Nevada	**85-0302351**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
410 North 44th Street, Suite 700, Phoenix, Arizona *(Address of Principal Executive Offices)*	**85008** *(Zip Code)*

Registrant s telephone number, including area code:

(602) 685-4000

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, No Par Value

(Title of Class)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

The aggregate market value of the voting stock held by non-affiliates of the Registrant as of December 11, 2001: Common Stock, no par value: $227.4 million.

On December 11, 2001, the Registrant had outstanding 33,048,988 shares of Common Stock.

Documents Incorporated by Reference

Documents	Form 10-K Reference
None	None

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MESA AIR GROUP, INC.

2001 FORM 10-K REPORT

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PART I

Forward-Looking Statements

This Form 10-K contains certain statements including, but not limited to, information regarding the replacement, deployment, and acquisition of certain numbers and types of aircraft, and projected expenses associated therewith; costs of compliance with FAA regulations and other rules and acts of Congress; the passing of taxes, fuel costs, inflation, and various expenses to the consumer; the relocation of certain operations of Mesa; the resolution of litigation in a favorable manner and certain projected financial obligations. These statements, in addition to statements made in conjunction with the words expect, anticipate, intend, plan, believe, seek, es and similar expressions, are forward-looking statements within the meaning of the Safe Harbor provision of Section 27A of the Securities Act of 1933 as amended and Section 21E of the Securities Exchange Act of 1934 as amended. These statements relate to future events or the future financial performance of Mesa and only reflect Management s expectations and estimates. The following is a list of factors, among others, that could cause actual results to differ materially from the forward-looking statements: changing business conditions in certain market segments and industries; changes in Mesa s code sharing relationships; the inability of either America West or US Airways to pay its obligations under the code share agreements; an increase in competition along the routes Mesa operates or plans to operate; material delays in completion by the manufacturer of the ordered and yet-to-be delivered aircraft; changes in general economic conditions; changes in fuel price; changes in regional economic conditions; Mesa s relationship with employees and the terms of future collective bargaining agreements; and the impact of current and future laws, additional terrorist attacks; Congressional investigations, and governmental regulations affecting the airline industry and Mesa s operations; bureaucratic delays; amendments to existing legislation; consumers unwilling to incur greater costs for flights; unfavorable resolution of negotiations with municipalities for the leasing of facilities; and risks associated with litigation outcomes. One or more of these or other factors may cause Mesa s actual results to differ materially from any forward-looking statement. Mesa is not undertaking any obligation to update any forward - looking statements contained in this Form 10-K.

Item 1. ***Business***

The terrorist attacks of September 11, 2001 had a significant impact on the operations of the Company. Following the attacks, the air transportation system was temporarily shut down, resulting in the cancellation of more than 3,300 Mesa Air Group flights. The cancelled flights and loss of consumer confidence in the airline industry resulted in lost revenue from these cancelled flights and lower load factors and revenue yield on flights operated. The Company was also impacted by certain costs that could not be avoided during the temporary shutdown.

As a result of the large financial losses attributed to the terrorist attacks on the United States that occurred on September 11, 2001, the Senate and House of Representatives of the United States of America passed, and the President signed into law H.R. 2926, the Air Transportation Safety and System Stabilization Act (the Airline Stabilization Act). The intent of the Airline Stabilization Act is to preserve the continued viability of the United States air transportation system. This legislation included support to passenger airlines in the form of a $4.5 billion grant, $10 billion in loan guarantees, and assistance with increased insurance costs. The $4.5 billion grant provided assistance for direct losses incurred as a result of the temporary shut down of the air transportation system and for incremental losses incurred through December 31, 2001 as a direct result of the terrorist attacks. The loan guarantees will be made to air carriers for which credit is not reasonably available and the guarantees are subject to certain conditions. Pursuant to the Airline Stabilization Act, the federal government has the authority to guarantee credit instruments issued by air carriers in an amount up to $10 billion. The Airline Stabilization Act allows the government to take an equity stake in the airlines receiving federal loan guarantees as collateral. The federal government is providing insurance assistance because, as a result of September 11, aviation insurers have significantly reduced the maximum amount of insurance coverage available to commercial air carriers for war-risk coverage. In addition, the insurance carriers have significantly increased the premiums for this coverage as well as for aviation insurance in general.

In addition, the federal government has issued war-risk coverage to U.S. air carriers for renewable 30-day periods. The Airline Stabilization Act also extended the due dates for excise and payroll tax deposits, and provides that any airline-related deposit required after September 10, 2001 and before November 15, 2001 will be treated as timely if the deposit is made on or before November 15, 2001.

General

Mesa Air Group, Inc. (Mesa or the Company) is a holding company whose principle subsidiaries operate as regional air carriers providing scheduled passenger and airfreight service, or as companies primarily in support of its operating airlines. The Company serves 153 cities in 38 states, the District of Columbia, Canada, and Mexico. At September 30, 2001, the Company operated a fleet of 116 aircraft and had approximately 832 daily departures.

Approximately 97% of the Company s consolidated passenger revenues for the fiscal year ended September 30, 2001, were derived from operations associated with code share agreements. The Company s subsidiaries have code share agreements with America West Airlines, Inc. (America West), Midwest Express Airlines, Inc. (Midwest Express), Frontier Airlines, Inc. (Frontier) and five separate code share agreements with US Airways, Inc. (US Airways). These code share agreements allow use of the code share partner s reservation system and flight designator code to identify flights and fares in computer reservation systems, permit use of logos, service marks, aircraft paint schemes and uniforms similar to the code share partners and provide coordinated schedules and joint advertising. Certain of these agreements also provide for generally favorable fixed fee and cost reimbursement terms that mitigate certain of the economic risks inherent in the Company s airline s operations.

In addition to carrying passengers, the Company carries freight and express packages on its passenger flights and has interline small cargo freight agreements with many other carriers. The Company also has contracts with the U.S. Postal Service for carriage of mail to the cities it serves and occasionally operates charter flights when aircraft are not otherwise used for scheduled service.

The Company s airline operations are conducted by three airline subsidiaries:

Mesa Airlines, Inc. (MAI) operates regional jet and turboprop aircraft as America West Express under a code share agreement with America West, primarily at America West s Phoenix and Columbus hubs. It also operates regional jets as US Airways Express under a code share agreement with US Airways, primarily at US Airways hubs in Philadelphia, Pittsburgh, Charlotte and Washington National Airports.

Air Midwest, Inc. (Air Midwest) operates Beechcraft 1900D 19-seat turboprops as US Airways Express under separate code share agreements with US Airways at US Airways hub operations in Pittsburgh, Philadelphia, Kansas City and Tampa. In February 2001, the Company entered into an agreement wherein Air Midwest s flights in Kansas City code share with Midwest Express Airlines as well as US Airways. Air Midwest also operates as Mesa Airlines from a hub in Albuquerque. The Albuquerque hub operation is an Independent Operation and is not subject to a code sharing agreement with a major carrier.

CCAIR, Inc. (CCAIR) operates turboprop aircraft as US Airways Express under a code share agreement with US Airways at US Airways Charlotte hub.

Unless the context indicates otherwise, the terms Mesa, the Company, we, us, or our, refer to Mesa Air Group, Inc. and its subsidiaries.

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Corporate Structure

Mesa is a Nevada corporation, with its principal executive office in Phoenix, Arizona.

In addition to its operating airline subsidiaries listed above, the Company also has the following other subsidiaries:

MPD, Inc., a Nevada corporation, doing business as Mesa Pilot Development and MPD ASU, operates the Company s training program for new pilots in conjunction with San Juan College in Farmington, New Mexico and Arizona State University in Phoenix, Arizona.

Regional Aircraft Services, Inc., a Pennsylvania corporation is a subsidiary of WestAir Holdings, Inc. and performs aircraft component repair and overhaul services.

Mesa Leasing, Inc., a Nevada corporation, was established to assist in the acquisition and leasing of aircraft.

MAGI Insurance, Ltd., a Barbados, West Indies based captive insurance company, was established for the purpose of obtaining more favorable aircraft liability insurance rates.

Ritz Hotel Management Corp., a Nevada Corporation, was established to facilitate the Company s acquisition and management of a Phoenix area hotel property used for crew accommodations.

FCA, Inc., a Nevada corporation (FCA), previously did business as Four Corners Aviation, a fixed based operation in Farmington, New Mexico. During fiscal 1999, substantially all of the assets of FCA were sold and FCA ceased operations.

WestAir Holding, Inc., a California corporation was owner of WestAir Commuter Airlines, Inc. a California corporation (WestAir). WestAir ceased operations in 1998.

UFLY, LLC (UFLY), a Delaware Limited Liability Company was established for the purpose of making strategic investments in common stock. The Company owns a 50% share of UFLY.

Aircraft in Operation

The following table sets forth, as of September 30, 2001, the Company s aircraft fleet (owned and leased) in operation by aircraft type.

	Canadair Regional Jet (CRJ)	Embraer Regional Jet (ERJ)	Beechcraft 1900D	DeHavilland Dash 8-100	DeHavilland Dash 8-200	British Aerospace Jetstream	TOTAL
USAirways Express	7	21	31	5		9	73
America West Express	25		3		12		40
Mesa Airlines (Ind. Opn.)			3				3
Total	32	21	37	5	12	9	116

The Changing Regional Airline Market and Code Share Agreements

Historically, the key characteristics of the regional airline market have included:

Operating feeder service to major airline hubs for connecting passengers under code share arrangements primarily in low density markets which are generally unattractive to major airlines;

Providing complimentary service in existing major airline markets by operating flights in scheduling gaps between those of the major airlines;

Operating turboprop aircraft in support of the major airlines   jet networks;

Prorating revenues for connecting customers between the regional and major airline while the regional airline operates in relative independence with respect to local customers in the regional markets, bearing the risks and reaping the rewards from the local customers, generally known as Prorate Agreements.

In recent years, new arrangements, generally known as Cost Plus Agreements, have developed between regional and major airlines. These agreements provide that all passenger revenues go to the major airline partner. In return, the major airline agrees to pay predetermined fees to the regional airline for operating an agreed upon number of aircraft, usually without regard to the number of passengers onboard. In addition, these agreements generally provide that certain variable costs, such as fuel and airport landing fees, be reimbursed 100% by the major airline. These arrangements, when properly structured, can be attractive to the regional airline in that the majority of the economic risks are assumed by the major airline partner, leaving the regional airline with often more predictable costs and revenues than under the Prorate Agreements.

The Company s airline subsidiaries have agreements with America West and US Airways to use those major carriers designation codes (commonly referred to as a code share). These code share agreements allow use of the code share partner s reservation system and flight designator code to identify flights and fares in computer reservation systems, permit use of logos, service marks, aircraft paint schemes and uniforms similar to the code share partners and provide coordinated schedules and joint advertising. The Company s passengers traveling on flights operated pursuant to code share agreements receive mileage credits in the respective frequent flyer programs of the Company s code share partners, and credits in those programs can be used on flights operated by the Company. Approximately 97% of the Company s consolidated passenger revenues for the year ended September 30, 2001, were derived from operations associated with code share agreements. The Company s subsidiaries have a code share agreements with America West, Midwest Express Airlines, Frontier Airlines and US Airways.

Both the America West code share agreement and the US Airways regional jet code share agreements are cost plus agreements. Under the terms of these cost plus agreements, the major carrier controls marketing, scheduling, ticketing, pricing and seat inventories. The Company receives a guaranteed payment for each departure operated and each mile flown, with certain costs, and reimbursement for expenses such as fuel and landing fees. Among other advantages, cost plus arrangements reduce the Company s exposure to fluctuations in passenger traffic and fare levels, as well as fuel prices.

For the fiscal year ended September 30, 2001, Mesa s America West Express operations, all of which were operated pursuant to cost plus agreements, represented approximately 44% of the Company s available seat mile capacity and 38% of its consolidated passenger revenue. For this same period, US Airways Express regional jet operations, all of which were also operated pursuant to a cost plus agreement, represented approximately 33% of the Company s available seat mile capacity and 27% of its consolidated passenger revenue. In total, operations under cost plus agreements accounted for approximately 77% of capacity, based on available seat miles, and approximately 65% of passenger revenues on a consolidated basis.

The Company s six US Airways turboprop code share agreements are prorate agreements, in which the Company is allocated a portion of each passenger s fare based on a standard industry formula and which require the Company to pay all the costs of transporting the passenger. For the fiscal year ended September 30, 2001, US Airways Express turboprop operations represented approximately 20% of the Company s available seat mile capacity and 32% of its consolidated passenger revenue.

Renewal of one code share agreement with US Airways does not guarantee the renewal of the other code share agreements with US Airways. Code share agreements provide for remaining terms of eleven years for America West, and from one to seven years for US Airways. Although the provisions of the code share agreements vary from contract to contract, generally each agreement is subject to cancellation should the applicable Company subsidiary fail to meet certain operating performance standards, breach of other contractual terms and conditions and, in the case of the US Airways code share agreements (other than the regional jet service agreement and the Kansas City code share agreement described below), upon six months notice by either party. The code share agreements contain provisions allowing the Company s code share partners to terminate the agreements upon certain potential operational or change in control events. The code share agreements do not prohibit the major carrier from having code share relationships with other regional carriers, although the Company does have exclusive rights from its code share partners on many of the routes served by the Company s subsidiaries. A termination, the inability of America West or US Airways to meet their financial obligations under these agreements or the expiration without renewal of the America West or US Airways Cost Plus agreements or more than one of the prorate agreements could have a material adverse effect on the Company s business prospects, financial condition and results of operations.

The various code share agreements are summarized as follows:

Agreement	Type	Expiration
America West	Cost Plus	2012(1)
US Airways:		
Kansas City, MO	Prorate	2005(3)
Pittsburgh, PA	Prorate	2004(3)
Philadelphia, PA	Prorate	2005(3)
Charlotte and Raleigh/ Durham, NC	Prorate	2003
New Orleans, LA	Prorate	2005(3)
Tampa and Orlando, FL	Prorate	2005(3)
Regional Jet Service	Cost Plus	2008(2)
Midwest Express	Prorate	2006(4)
Frontier	Prorate	2007(5)

(1) In March 2001, the Company and America West entered into a new Cost Plus Agreement to expand the number of regional jets operated from 22 to 65 and extend the term of the agreement to April 2012, or eight years beyond the delivery date of the last aircraft.

(2) In November 1999 and October 2000, the Company and US Airways amended the US Airways regional jet service Cost Plus Agreement. The amendments expanded the number of regional jets operated from 14 to 32 and extended the term from 2004 to 2008. In addition, the amendments eliminated the ability of US Airways to terminate the Cost Plus Agreement without cause.

(3) In October 2000, the Company and US Airways amended three of its revenue prorate agreements. The Kansas City agreement was extended from 2000 to 2005. In addition, the agreement was amended to eliminate the ability of either party to terminate the agreement without cause and permit the Company to add additional code share partners in Kansas City. The other two prorate agreements were extended by one year beyond their previous expiration dates.

(4) In February 2001, the Company entered into a new agreement with Midwest Express Airlines, Inc. (Midwest Express) to add the Midwest Express designation code to the Company s operations in Kansas City. The agreement covers 12 cities already served by ten 1900D aircraft.

(5) In September 2001, the Company entered into an agreement with Denver based Frontier Airlines to form a regional jet code share relationship. Under the terms of the agreement, Frontier will market and sell flights operated by Mesa as Frontier JetExpress. The code share is anticipated to begin during the first calendar quarter of 2002 and will initially include the operation of at least five 50-passenger Bombardier CRJ-200 regional jets.

Fleet Plans and Aircraft Manufacturer Relationships

ERJ Program

In January 2000, Mesa entered into an agreement with Empresa Brasiliera de Aeronautica SA (Embraer) to acquire 36 50-passenger Embraer ERJ-145 regional jets. Deliveries began late in the third quarter of fiscal 2000 and will continue into early 2003. Mesa introduced the ERJ-145 aircraft into revenue service in the third quarter of fiscal 2000 as USAirways Express. Mesa has moved several of the CRJ regional jets currently flying as USAirways Express to America West Express and replaced them with ERJ-145 s as

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deliveries took place. The Company also intends to move several CRJ regional jets currently flying as USAirways Express to Frontier JetExpress and replace them with ERJ-145 s as well. As of September 30, 2001, the Company had taken delivery of 21 ERJ-145 s, which have been financed as operating leases. In conjunction with this purchase agreement, Mesa has $10.9 million on deposit with Embraer, which is included with lease and equipment deposits.

CRJ Program

In August 1996, the Company entered into an agreement with Bombardier Regional Aircraft Division (BRAD) to acquire 16 CRJ 50-passenger jet aircraft. The agreement also granted the Company an option to acquire an additional 16 jet aircraft and provided for additional rolling options to acquire a third block of 16 aircraft. In fiscal 1997, the Company exercised options to purchase 16 of the 32 CRJ aircraft reserved under the option provisions of the BRAD purchase agreement. In connection with the 32 CRJ aircraft, all are currently under permanent financing as operating leases with terms of 16 1/2 to 18 1/2 years. In fiscal 1998, BRAD canceled the third block of rolling options.

In May 2001, the Company entered into an agreement with BRAD to acquire 20 64-seat CRJ-700s, and 20 84-seat CRJ-900s. Deliveries of the CRJ-700 and CRJ-900 will commence in the third quarter of fiscal 2002 and the second quarter of fiscal 2003, respectively. Mesa will be the launch customer of the CRJ-900. In addition to the firm orders, Mesa has an option to acquire an additional 80 CRJ-700 and CRJ-900 regional jets. In conjunction with this purchase agreement, Mesa has $8.3 million on deposit with BRAD, which is included with lease and equipment deposits.

The following summarizes the Company s jet fleet status and current fleet expansion plans for the periods indicated:

	CRJ-200	CRJ-700 Firm Orders	CRJ-900 Firm Orders	CRJ-700 Options	CRJ-900 Options	ERJ-145 Firm Orders	Cumulative Total
Delivered:							
At 9/30/2001	32					21	53
Scheduled deliveries:							
Fiscal 2002		5				11	69
Fiscal 2003		10	8			4	91
Fiscal 2004		5	12				108
Fiscal 2005				3	3		114
Fiscal 2006				12	12		138
Fiscal 2007				5	5		148
Total	32	20	20	20	20	36	

Beechcraft 1900D

In fiscal 1999, the Company announced its intention to dispose of 30 excess 1900D aircraft. As of September 30, 2001, the Company had disposed of 17 of such aircraft. During the second quarter of fiscal 2001, the Company continued its turboprop restructuring plan by announcing a plan to retire an additional eight B1900 aircraft. Under an agreement with Raytheon Aircraft Corporation (RAC), the Company has the right to return 15 B1900D aircraft, ten of which may be returned immediately and five no earlier than October 2002. The Company is seeking proposals for the disposition of the remaining six B1900 aircraft. Mesa further reduced its fleet by returning two aircraft to the lessor upon expiration of their leases in the second quarter of fiscal 2001.

Marketing

The Company s flight schedules are structured to facilitate the connection of its passengers with flights of its code share partners at their hub airports and to maximize local and connecting service to other carriers in Albuquerque.

Under the Company s US Airways Express turboprop operations, the Company s market selection process follows an in-depth analysis on a route-by-route basis and is followed by a review and approval process in a joint effort with US Airways regarding the level of service and fares. The Company believes that this selection process enhances the likelihood of profitability in a given market.

Under the America West Express Contract Agreement and the US Airways Express regional jet Contract Agreement, market selection, pricing and yield management functions are performed by America West and US Airways, respectively. The Company s role is simply to operate its fleet in the safest and most reliable manner in exchange for fees paid under a generally fixed payment schedule. The Company intends to expand its operations performed pursuant to these Contract Agreements.

Under the Company s code share agreements, the code share partner coordinates advertising and public relations within their respective regions. In addition, the Company s prorate traffic is impacted by the major airline partners advertising programs in regions outside those served by the Company, with the major partners customers becoming customers of the Company as a result of through fares. Under Prorate code share arrangements, the Company s passengers also benefit from through fare ticketing with the major airline partners and greater accessibility to the Company s flights on computer reservation systems and in the Official Airline Guide.

The Company s Prorate Agreement and Independent Operation flights are promoted through, and the Company s revenues are generally believed to benefit from, listings in computer reservation systems, the Official Airline Guide and through direct contact with travel agencies and corporate travel departments. The Company participates in shared advertising with resort and rental property operators and ski areas in leisure markets in which it operates. The Company s non-code share operation utilizes SABRE, a computerized reservation system widely used by travel agents, corporate travel offices and other airlines. The reservation systems of the Company s code share partners are also utilized in each of the Company s other operations through their respective code share agreements. The Company also pays booking fees to owners of other computerized reservation systems based on the number of independent and prorate passengers booked by travel agents using such systems. The Company believes that it has good relationships with travel agents serving its passengers.

Fares and Contract Agreement Flying

The Company has increasingly relied on Contract Agreements with its code share partners to generate revenue. All of the Company s America West Express and US Airways Express regional jet operations are on a contract basis. The percentage of revenue generated under Contract Agreements is expected to increase in future years as the Company continues to add regional jets to its America West Express and US Airways Express operations and reduce the number of Beech 1900D and Jetstream Super 31 aircraft in operation. In fiscal 2001, the Company generated approximately 65% of its total passenger revenue pursuant to Contract Agreements.

Competition

The airline industry is highly competitive and volatile. Airlines compete in the areas of pricing, scheduling (frequency and timing of flights), on-time performance, type of equipment, cabin configuration, amenities provided to passengers, frequent flyer plans, travel agent commissions and the automation of travel agent reservation systems. Further, because of the Airline Deregulation Act, airlines are currently free to set prices and establish new routes without the necessity of seeking governmental approval. At the same time, deregulation has allowed airlines to abandon unprofitable routes where the affected communities will not be left without air service.

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The Company believes that the Airline Deregulation Act facilitated the Company s entry into scheduled air service markets and allows it to compete on the basis of service and fares, thus causing major carriers to seek out further contractual agreements with carriers such as the Company as a way of expanding their respective networks. However, the Airline Deregulation Act makes the entry of other competitors possible, some of which may have substantial financial resources and experience, creating the potential for intense competition among regional air carriers in the Company s markets.

The Company believes its code share agreements provide a significant competitive advantage in hub airports where its major partner has a predominant share of the market. The ability to control connecting passenger traffic by offering superior service creates difficulty for other regional airlines wishing to compete at such hubs. In addition to enhanced competitiveness offered by the code share agreements, the Company competes with other airlines by offering frequent flights, flexible schedules and numerous fare levels.

Fuel

Historically, the Company has not experienced problems with the availability of fuel, and believes that it will be able to obtain fuel in quantities sufficient to meet its existing and anticipated future requirements at competitive prices. Standard industry contracts generally do not provide protection against fuel price increases, nor do they ensure availability of supply. However, the Company s code share agreement with America West and the regional jet service agreement with US Airways allow fuel used in the performance of the agreements to be billed to the code share partner, thereby reducing the Company s exposure to fuel price fluctuations. In fiscal 2001, approximately 75% of the Company s fuel was associated with the Company s America West code share and US Airways regional jet service agreements. A substantial increase in the price of jet fuel, to the extent the Company s fuel costs are not reimbursed, or the lack of adequate fuel supplies in the future may have a material adverse effect on the Company s business, financial condition, results of operations and liquidity.

Maintenance of Aircraft and Training

All mechanics and avionics specialists employed by the Company have the appropriate training and experience and hold the required licenses issued by the Federal Aviation Administration (FAA). Using a combination of FAA-certified maintenance vendors and its own personnel and facilities, the Company maintains its aircraft on a scheduled and as-needed basis. The Company emphasizes preventive maintenance and inspects its aircraft engines and airframes as required. The Company also maintains an inventory of spare parts specific to the aircraft types it flies. The Company provides periodic in-house and outside training for its maintenance and flight personnel and also takes advantage of factory training programs that are offered when acquiring new aircraft.

Insurance

The Company carries types and amounts of insurance customary in the airline industry, including coverage for public liability, passenger liability, property damage, product liability, aircraft loss or damage, baggage and cargo liability and workers compensation.

As a result of the terrorist attacks on September 11, 2001, aviation insurers have significantly reduced the maximum amount of insurance coverage available to commercial air carriers for war-risk coverage. In addition, the insurance carriers have significantly increased the premiums for this coverage as well as for aviation insurance in general. Under the terms of the Company s code share agreement with America West, and its regional jet service agreement with US Airways, insurance costs are reimbursed. Given the significant increase in insurance costs, the federal government is providing insurance assistance under the Air Transportation Safety and System Stabilization Act. In addition, the federal government has issued war-risk coverage to U.S. air carriers for renewable 30-day periods. However, the availability of aviation insurance is not guaranteed and the inability of the Company to obtain such coverage may result in the grounding of its aircraft.

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Employees

As of September 30, 2001, the Company employed approximately 2,800 employees. The Company s continued success is partly dependent on its ability to continue to attract and retain qualified personnel. Historically, the Company has had no difficulty attracting qualified personnel to meet its requirements. The Company believes that relations with its employees are favorable.

Pilot turnover at times is a significant issue among regional carriers when major carriers are hiring experienced commercial pilots away from regional carriers. The addition of aircraft, especially new aircraft types, can result in pilots upgrading between aircraft types and becoming unavailable for duty during the extensive training periods required. No assurances can be made that pilot turnover and unavailability will not again be a significant problem in the future, particularly if major carriers expand their operations. Similarly, there can be no assurance that sufficient numbers of new pilots will be available to support any future growth.

During December 1996, the Company reached a five-year agreement, expiring in December 2001, with the Air Line Pilots Association (ALPA) for a single pilot contract for MAI and Air Midwest. The Company expects to commence contract negotiations with pilots for MAI and Air Midwest in early 2002. Air Midwest mechanics are represented by the International Association of Machinists (IAM). The current agreement with the IAM is amendable on March 31, 2002. MAI s flight attendants are represented by the Association of Flight Attendants (AFA). The AFA contract is amendable on June 13, 2003.

CCAIR has three organized employee groups. ALPA represents the pilots, AFA represents the flight attendants and the International Brotherhood of Teamsters (Teamsters) represents the mechanics and stock clerks. The ALPA agreement was renewed on November 6, 1998, and becomes amendable on October 31, 2002. The AFA agreement was renewed on May 16, 1996, and becomes amendable on June 13, 2003. The Teamsters mechanics contract was ratified on July 15, 1998, and becomes amendable on December 31, 2001. The Teamsters stock clerks contract was ratified July 31, 2000 and becomes amendable on December 31, 2003.

No other Mesa subsidiaries are parties to any other collective bargaining agreement or union contracts.

Approximately 60% of the Company s workforce is subject to collective bargaining agreements.

Essential Air Service Program

The Essential Air Service program administered by the United States Department of Transportation (DOT) guarantees a minimum level of air service in certain communities, predicated on predetermined guidelines set forth by Congress. Based on these guidelines, the DOT will subsidize air service to communities that might not otherwise have air service. The Company services 15 such cities for an annual subsidy of approximately $6.6 million. Funding for this program is currently being evaluated in Congress and there is no guarantee that the Company will continue to receive subsidies for the cities it serves. If the funding under this program is terminated for any of the cities served by the Company, there is no assurance that the Company would continue to fly in these markets, and as a result, the Company would be forced to find alternative uses for the aircraft affected.

Regulation

As an interstate air carrier, the Company is subject to the economic jurisdiction, regulation and continuing air carrier fitness requirements of the DOT. Such requirements include minimum levels of financial, managerial and regulatory fitness. The DOT is authorized to establish consumer protection regulations to prevent unfair methods of competition and deceptive practices, to prohibit certain pricing practices, to inspect a carrier s books, properties and records, and to mandate conditions of carriage. The DOT also has the power to bring proceedings for the enforcement of air carrier economic regulations, including the assessment of civil penalties, and to seek criminal sanctions.

The Company is subject to the jurisdiction of the FAA with respect to its aircraft maintenance and operations, including equipment, ground facilities, dispatch, communication, training, weather observation,

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flight personnel and other matters affecting air safety. To ensure compliance with its regulations, the FAA requires airlines to obtain an operating certificate, which is subject to suspension or revocation for cause, and provides for regular inspections.

Effective March 1997, the FAA required that regional airlines with aircraft of 10 or more passenger seats operating under FAR Part 135 rules to begin operating those aircraft under FAR Part 121 regulations. The Company, as one of the largest regional airlines operating under FAR Part 135 regulations, completed the transition to Part 121 within the FAA s deadline. These requirements have resulted in a significant increase in the Company s costs, affecting the Company s ability to profitably serve certain markets. Such increased costs are primarily related to additional training, dispatch and maintenance procedures. The Company continues to attempt to minimize the cost of these new operating procedures while fully complying with FAR Part 121 operating requirements.

The Company is subject to various federal and local laws and regulations pertaining to other issues of environmental protocol. The Company believes it is in compliance with all governmental laws and regulations regarding environmental protection.

The Company is also subject to the jurisdiction of the Federal Communications Commission with respect to the use of its radio facilities and the United States Postal Service with respect to carriage of United States mail. Local governments in certain markets have adopted regulations governing various aspects of aircraft operations, including noise abatement and curfews.

Item 2. ***Properties***

The Company s primary property consists of the aircraft used in the operation of its flights. The following table lists the aircraft owned and leased by the Company as of September 30, 2001.

	Number of Aircraft				
Type of Aircraft	**Owned**	**Leased**	**Total**	**Operating on Sept. 30, 2001**	**Passenger Capacity**
Canadair Regional Jet		32	32	32	50
Embraer Regional Jet		21	21	21	50
Beechcraft 1900D	51	8	59	37	19
Jetstream Super 31		9	9(1)	9	19
Dash 8-100		7	7	5	37
Dash 8-200		12	12	12	37
Embraer EMB-120		6	6		30
Total	51	95	146	116	

(1) At September 30, 2001, Management decided to stop operating these aircraft effective February 1, 2002.

See Business Airline Operations and MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS Liquidity and Capital Resources for a discussion regarding the Company s aircraft fleet commitments.

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In addition to aircraft, the Company has office and maintenance facilities to support its operations. The facilities are as follows:

Type	Location	Ownership	Approximate Square Feet
Administrative/Dispatch	Phoenix, AZ	Leased	21,000
Flight Operations/Training/Admin Records/Technical Publications	Phoenix, AZ	Leased	27,000
Hangar	Farmington, NM	Leased	30,000
Engine Shop	Farmington, NM	Leased	6,000
Hangar	Fresno, CA	Leased	18,500
Hangar/ Office	Wichita, KS	(1)	30,000
Hangar	Jamestown, NY	Leased	30,000
Hangar/ Office	Dubois, PA	Leased	23,000
Hangar	Reading, PA	(1)	56,250
Hangar/ Office	Grand Junction, CO	(1)	32,770
Office	Charlotte, NC	Leased	11,000
Hangar	Charlotte, NC	Leased	30,000