



..... Airport Policy Report ..... 



A Playbook for Successfully Reforming the FAA and Airport Programs



Meeting the Needs of Airports in Today's Aviation System



A New Airport-Airline Partnership



## Welcome to the Second Volume of the *Airport Policy Report*

The possibility of 2015 turning out to be an historic year for our aviation system has increased since the first edition of the *Airport Policy Report*. The House of Representatives and the Senate are each holding hearings on what could turn out to be dramatic reforms of the Federal Aviation Administration (FAA) and its programs.

The *Airport Policy Report* is written and edited by Stephen D. Van Beek, Vice President of Airport Advisory Services, with assistance from consultants in ICF's aviation, transportation and federal practices.

The first three volumes are:

**Volume One:** *A Playbook for Successfully Reforming the FAA and Airport Programs*

**Volume Two:** *Meeting the Needs of Airports in Today's Aviation System*

**Volume Three:** *A New Airport-Airline Partnership*

## Meeting the Needs of Today's System and Airports

If fundamental reform of the FAA occurs in 2015 or 2016, the industry and the communities that rely on the agency would benefit substantially. The principal reason is that the policies and funding architectures for aviation are relics of a different era—one created prior to the recent consolidation of the U.S. airline industry, the terrorist attacks of September 11, and the increasing globalization of the industry.

As result, policies that govern air traffic management, set the hodgepodge of fees and taxes which pay for the vast majority of air traffic services, and apply to our nation's airports date from the 1970s, 1980s, and 1990s. While these laws and regulations often served the national aviation system well for a quarter-century, changes in the industry mean these legacy policies now threaten our nation's global leadership in aviation.

Fundamental FAA reform requires that policy makers step in and play a constructive and enabling role in finding solutions. The underlying principles for reform should be to:

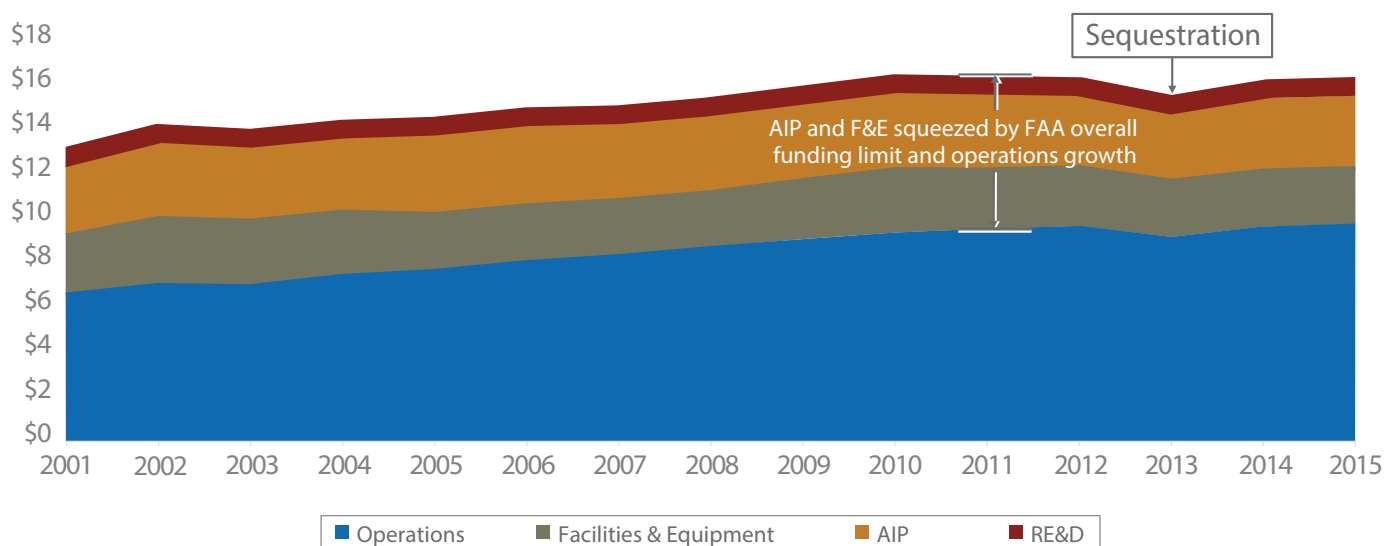
1. Remove aviation's extreme vulnerability to federal political and budgetary failure.
2. Allow the aviation industry to self-fund vital services such as air traffic, certification, and airports.
3. Focus the new limited federal role on the public goods of the system, including overseeing safety, the environment, and consumer protection as well as supporting smaller airports.



The first task is to reform industry finances. The Airport and Airway Trust Fund (AATF) continues to provide the vast majority (75 to 90 percent) of funding for system needs and airports. As detailed in the first *Airport Policy Report*, however, the AATF no longer provides a steady and sustainable flow of revenues to support aviation programs. Reasons include:

- Severe pressure on federal domestic discretionary spending that restrains aviation spending, even programs ostensibly funded and “guaranteed” by the AATF.
- Growth in the FAA operations account, which together with the overall cap on the agency budget is causing the Facilities and Equipment (F&E) and AIP to be squeezed (see accompanying graph).
- Decreased growth in revenues from AATF’s largest contributor, the federal 7.5 percent excise tax on airline tickets as airlines charge separately (off the ticket) for services such as baggage and ticket changes, thereby decreasing the per-passenger revenue return to pay for system needs.

**FAA Finances: Major Program Functions Fiscal Year 2001-2015**



Source: Van Beek, “FAA and Aviation Policy Reform: Now is the Time” FAA MAC Joint Meeting, January 29, 2014 (updated January 2015)



Some critics of reform have claimed that FAA finances are just fine, citing a “\$6 billion surplus” in the AATF. That \$6 billion represents approximately 137 days of cash on hand for the FAA at a time when the agency has faced about every example of budgetary crisis and operates under the restrictions of the government’s Anti-Deficiency Act. Many airports holding this proportion of cash would face technical default under their bond covenants. To maintain a 24/7 operation and invest in multiyear air traffic and airport projects, the FAA and other infrastructure providers must have sustainable funding and some form of “rainy-day” capital.

## New Ways of Delivering and Paying for Aviation

As federal policy makers have fiddled over the last decade, many other nations with mature aviation systems have undergone a process of reform. Components typically have included separating the operations and investments in air traffic control from their safety regulator, freeing modern and commercial airports from state dependence and heavy-handed regulation by enabling head taxes and privatization, and reserving public funding and regulation for those parts of the system where the market cannot either govern itself or pay for public goods.

Fortunately, many stakeholders and, increasingly many policy makers, are discussing ways in which the United States can employ the best of these examples and tailor them to our unique geography, sheer size of our system, and our aviation culture. Under these best practices, the new roles and funding mechanisms would have the following attributes:

1. **User Charges for Air Traffic Services:** Airlines and other users of the nation’s airspace would pay for services used. This business-to-business (B2B) transaction would allow the vast majority of ticket taxes to be eliminated, while the costs would flow to user balance sheets, incentivizing efficient use.
2. **Airport Infrastructure:** A new mix of self-help investment strategies are available to allow the busiest airports to recover their costs, thereby tailoring industry support to those airports that require assistance—those serving many remote, rural, and smaller communities.
3. **Certification Fee-for-Service:** Where possible, manufacturers and other beneficiaries of this service would pay directly for services, enabling faster approvals and removing their vulnerability to budget interruptions, which delay introduction of valuable new aircraft, products and clearances;
4. **Safety and Other Public Goods:** Options for these functions include funding safety and other public services out of the general fund or a standalone industry charge—the latter of which would effectively remove industry dependence on federal support and guarantee the continuity of services even when our nation’s capital is not working.

Seen in this light, airports offer a constructive contribution for reform. Reforms can reduce industry support for airports that do not require subsidies, while focusing on a recalibrated AIP program for those airports that do.

There are a number of ways to package airport reforms, but one sensible trade-off, which would work for airports, airlines and passengers, is to include a recalibrated AIP, in tandem with an increase in the authorized level of the passenger facility charge (PFC).



## What Is a Smaller Airport?

When I speak to airport boards and communities about smaller airports, no topic generates as much confusion as the FAA's categories for airport size (i.e., large hubs, medium hubs, smaller hubs, and non-hubs). These definitions, based on an airport's share of national traffic, have no meaning outside a federal grant program. The term "hub" causes frequent and understandable confusion. As part of FAA reform, airports should be re-categorized to align with their role in the national system. In addition to lessening confusion, a change will enable policy makers and the FAA to better target PFC authority and AIP funding to the airports where they best fit.

This trade-off—a higher PFC for lower AIP funding—first appeared with the passage of the Airport Noise and Capacity Act of 1990 and appeared again in 2000 when President Clinton signed into law the Wendell H. Ford Aviation Investment and Reform Act for the 21<sup>st</sup> Century (AIR-21).

President Obama recommended one version of this budget-saving deal in the FAA's Fiscal Year 2016 budget, enabling nearly a half-billion dollar savings in AATF revenues in exchange for raising the PFC ceiling from today's maximum (part of AIR-21) of \$4.50 to \$8.00 (a figure that mirrors the increase in construction costs since 2000). Depending on how policy makers would restructure a new AIP and the level of PFC, the amount of savings could even approach \$1 billion.

Smaller airports that are challenged to pay for all of their capital needs would receive the lion's share of AIP. Airline consolidation (made possible by federal exemptions to antitrust policies), the gradual disappearance of smaller aircraft, and high fuel costs are all responsible for the reduction in traffic to smaller airports. The decline in traffic and continued uncertainty make it impossible for smaller airports to raise enough funds from PFCs and rates and charges to pay for their operations and capital investments. In addition, unlike their larger airport counterparts, their lower passenger levels make most of them too big a risk to raise money from the capital markets.

While some would like to reduce capital grants for smaller airports or subject AIP to the uncertainties of taxpayer funding, such reforms would jeopardize access to the national aviation system for commercial airline service as well as for general aviation. Robbing remote, rural, and smaller communities of aviation's economic benefits would not only be bad policy but also bad politics in a Congress where representatives and senators will protect "their airport."

Even though the trade-off between reduced AIP funding and a higher PFC appears to make good sense and enable system-enhancing reforms, it runs counter to current airline lobbying talking points. Representatives of airlines continue to oppose any PFC increase—just as they have since 1990 when PFCs were first introduced. Conventional wisdom in our nation's capital today suggests that airline opposition means airports have no hope for a PFC increase.



## Why Airlines May Reconsider

Increasingly, however, that wisdom appears questionable. Why? At this point in the legislative process, when congressional committees are just beginning to mark up FAA reauthorization, aviation interests, including airlines, are not in a position to calculate how all the moving parts of reform would fit together. However, if Congress proceeds with reform and stakeholders believe there is a serious chance for significant change, all political calculations, including those from the airlines, will have to be reassessed. Airlines, for example, would benefit from FAA transformational reform in several ways:

1. Previous ticket taxes, including the excise tax, international arrivals tax, cargo tax, and fuel tax, would all go away as payment for air traffic becomes a B2B transaction.
2. Customers, including the airlines, would gain a seat at the governing table for a new air traffic organization, enabling them to help in defining the requirements for an air traffic system and craft equitable ways to pay for the services.
3. PFCs collected at the major airports would “stay at home,” dedicated to projects the airlines use and generally support. If a PFC increase reduces the amount of AIP funding necessary to recover from some form of small airport fee, airlines would be better off.

If this political calculus sounds far-fetched, no less an airline advocate than Robert L. Crandall, the former CEO of American Airlines, spoke in favor of just these principles at a recent Wing’s Club event in New York City (excerpted in a recent article<sup>1</sup>).

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*“Doing a deal to swap higher PFCs for the AIP—and building in provisions to give airlines some protection from airport grandiosity—would be a good deal for the airports, airlines, passengers and Mr. and Mrs. America who do not want to travel through run-down, out-of-date airport facilities.”*

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<sup>1</sup> Robert Crandall, “Don’t Blow Our Shot at FAA Financing Reform,” Aviation Week & Space Technology, April 3, 2015, p. 74; retrieved from <http://aviationweek.com/commercial-aviation/opinion-don-t-blow-our-shot-faa-financing-reform>.



## Paying for Safety, Smaller Airports and Other Public Goods

If user charges pay for air traffic control, larger airports, and at least a portion of certification services then that leaves only a smaller AIP, the FAA's safety program, and a few other functions such as aviation research, requiring funding solutions.

Today, FAA collects a \$4.00 segment fee (annually adjusted for inflation) that applies to almost all domestic segments flown. That fee generates a sufficient amount of capital to pay for a recalibrated AIP and, if international enplanements are included and the fee is raised to \$5.00, enough to pay for the balance of FAA programs.

Removing the FAA and aviation services from any taxpayer support would free the industry from its current political vulnerability, allowing service delivery to be more efficient, expeditious, and equitable. Although the FAA and aviation would no longer receive the 8 to 25 percent of the FAA's budget that comes from the general fund (recently aviation has been on the low end of that range), most believe that the new policy and funding architecture would generate greater cost savings than the revenues lost from taxpayer support. While a 3-5 year transition period would be required to stand up the new entity and transition the finances, at the end of the process policymakers would be able to say that they produced historic change for our aviation system.

*In the third issue, we will discuss the possibilities of a new airport-airline partnership on issues such as security, funding of infrastructure, air service, and landlord-tenant relations.*



Dr. Van Beek is a well-known industry expert who was recently a member of the Federal Aviation Administration's Management Advisory Council; served as an Executive Vice President for Airports Council International—North America and as the Associate Deputy Secretary of the U.S. Department of Transportation. Dr. Van Beek and ICF International offer a wide variety of business planning and policy services for airports. For more information, please contact Steve by email at [steve.vanbeek@icfi.com](mailto:steve.vanbeek@icfi.com).

## About ICF International

ICF International (NASDAQ:ICFI) provides professional services and technology solutions that deliver beneficial impact in areas critical to the world's future. ICF is fluent in the language of change, whether driven by markets, technology, or policy. Since 1969, we have combined a passion for our work with deep industry expertise to tackle our clients' most important challenges. We partner with clients around the globe—advising, executing, innovating—to help them define and achieve success. Our more than 5,000 employees serve government and commercial clients from more than 70 offices worldwide. ICF's website is [www.icfi.com](http://www.icfi.com).

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