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THE FINANCIAL CONDITION OF THE AVIATION TRUST FUND: ARE REFORMS NEEDED?

(109–16)

HEARING

BEFORE THE

SUBCOMMITTEE ON AVIATION

OF THE

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

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THE FINANCIAL CONDITION OF THE AVIATION TRUST FUND: ARE REFORMS NEEDED?

Wednesday, May 4, 2005

HOUSE OF REPRESENTATIVES, COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE, SUBCOMMITTEE ON AVIATION, WASHINGTON, D.C.

The committee met, pursuant to call, at 10:06 a.m., in room 2167, Rayburn House Office Building, Hon. John Mica [chairman of the subcommittee] presiding.

Mr. MICA. I would like to call the House Aviation Subcommittee hearing to order. I welcome everyone today. The order of business is going to be opening statements by members, and then we have two panels of witnesses. The subject of today's hearing is the financial condition of the Aviation Trust Fund and what reforms are needed. I will begin with my comments, and then yield to other members.

Today's hearing will focus, as I said, on the condition of the Aviation Trust Fund, in both the short term and also for the long term. We have to ask ourselves some questions. One of them is, is our current system of financing our Nation's air traffic control system and the Federal Aviation Administration broken?

Trust Fund revenues are down significantly from the levels that were projected prior to the terrorist attacks of September 11, 2001. The 9/11 attacks, combined with weak economic conditions and lower airfares, resulted in three consecutive years of declining trust fund revenues. It went from $10.5 billion in fiscal year 2000, to $9.3 billion in fiscal year 2003.

Although revenues now appear to be on an upward trend once again, the uncommitted cash balance in the Trust Fund has been dramatically reduced, from $7.3 billion at the end of fiscal year 2001, to only $2.4 billion at the end of 2004.

This raises the short-term question, given the uncertainty surrounding these revenue projections and the possibility that revenues will be even less than currently forecast, what if anything should be done now to ensure that the uncommitted cash balance does not reach zero before the next aviation reauthorization bill, which will take effect in fiscal year 2008?

There is also a long-term issue of how to best finance our aviation system needs for the future. The cost of modernizing our system and expanding capacity to meet future travel demand we know will be significant. Yet, the Administration's current budget proposes to cut funding for aviation capital investments and some other critical areas.

As the Department of Transportation Inspector General Ken Mead testified before this Subcommittee last month, the current budget level for the FAA capital account is not sustainable. We will hear from him again today.

With the funding level currently proposed by the Administration, at the level they are proposing, there is little room for the FAA to pay for both current systems and simultaneously take on any new initiatives. This is not acceptable, I think, for anyone here.

The Transportation and Infrastructure Committee has long worked to ensure that user revenues collected by the Transportation Trust Funds are actually made available to be invested for the purposes for which they are collected.

The committee addressed this issue for the Aviation Trust Fund most recently in AIR 21 and also in Vision 100, by requiring Trust Fund revenues to first be used to fully fund the FAA's capital programs before being used to pay any portion of the FAA's operating costs.

Unfortunately, the President's budget has routinely ignored this requirement by proposing to cut funding for FAA's capital programs below the authorized levels, and use excessive amounts from the Trust Fund balance, to pay for FAA operations. Clearly, we need some reforms to ensure that aviation capital needs are not shortchanged in a budget process that tends to defer long-term capital investments in order to meet short-term operating needs.

In preparation for the next reauthorization bill, when our current aviation excise taxes must either be extended or replaced, Transportation Secretary Mineta and FAA Administrator Blakey have called for a dialogue on alternative ways to finance our aviation system in the future. Hopefully, we will hear some of those comments from the administrators today.

The FAA believes that certain industry trends, such as lower airfares and the use of smaller aircraft, will exacerbate the mismatch between its workload and also its projected revenue for the future.

Cost-based user fees are often mentioned as one way to link aviation revenues more closely to FAA's costs, and potentially to its funding. Cost-based user fees have been recommended for the FAA by various Commissions in the past, and most recently by the Mineta Commission, I believe, in 1997.

Last month, the Aviation Subcommittee held a hearing on how other countries provide air traffic control services. Many countries now rely on user fees for providing air navigation service to aircraft. In general, these countries use a formula based upon aircraft weight and distance flown, as outlined in ICAO standards.

With the recommendations of the Mineta Commission, and the widespread use of user fees in other countries, we probably should take some time to review the possibility of converting to a user fee system here in the United States. I am sure that will be part of our discussion. As part of this process, we need to look at who is paying what, and how what they are paying matches with the FAA's cost of providing services to each user group.

We also need to raise the question of what is the appropriate General Fund contribution to the FAA's budget. How much of what FAA does is in the national interest versus for the benefit of indi-

vidual users? What services, if any, do policymakers wish to subsidize? These are all important questions.

We also need to look at the idea of bonding, which is seen by some as an attractive way to modernize our air traffic control system without requiring the user to pay all of the investment up front.

While this may make sense if the FAA had a well-defined investment plan that would provide to our aviation system users a rate of return sufficient to repay the debt, it is by no means the only "silver bullet" to solve the problem.

It will not provide free money. There would likely be no budget scoring advantage to this approach, compared to traditional appropriations, at least the way we now score it.

In addition, it would likely cost more to borrow funds in the private market than it would for the Treasury to finance the investments that are needed directly.

We need to ask many questions today, and hopefully get answers from some of the witnesses we have before us. I commend the Department of Transportation and FAA Administrator Blakey for helping start this dialogue, and I look forward to hearing the views of all segments of the aviation industry who will be represented and speak here today. I am pleased now to yield to our Ranking Member, Mr. Costello.

Mr. COSTELLO. Mr. Chairman, thank you, and I want to thank you for calling this important hearing today on the financial condition of the Aviation Trust Fund. I do have a lengthy statement that I will submit for the record, and I do have some comments on today's hearing.

First, there is no disagreement that the Trust Fund's uncommitted balance has declined over the past few years. As you noted in your opening statement, at the end of fiscal year 2000, the Trust Fund's uncommitted balance was a little more than $7 billion. At the end of fiscal year 2004, the Trust Fund's uncommitted balance fell to just under $2.5 billion.

As Mr. Mead, the Inspector General, will testify here today, Trust Fund revenue estimates for the last few years have been overly optimistic. For fiscal year 2004, the actual receipts plus interest credited to the Trust Fund was 12 percent less than projected. The shortfall between projected revenues and actual revenues has been made up from the Trust Funds uncommitted balance.

A major question before the Subcommittee today is, are the FAA's revenue projections reliable? To its credit, the FAA has initiated an independent review of its aviation activity and revenue forecast system. The downturn in passenger travel after September 11th clearly had an impact on the Trust Fund; and also changes within the airline industry are affecting Trust Fund revenues, as well as the FAA's ability to forecast those revenues.

The growth of low cost carriers and fare reductions by legacy carriers have driven passenger ticket tax returns that account for about 50 percent of annual trust fund revenue. The FAA is predicting that the Trust Fund revenue will increase over the next few years. Yet even with this projected increase, the FAA believes that

revenues would be less than we forecast when Vision 100 was enacted in 2003.

I believe that Dr. Dillingham of the GAO will testify this morning that if revenues are 10 percent less than now projected under the current law, the Trust Fund's uncommitted balance would reach zero by 2007. If traffic is less than expected or fares drop, we will need to consider measures to address the shortfall, which could include cutting the FAA's programs, raising taxes, or obtaining a larger General Fund contribution.

As to the possibility of cutting the FAA's programs, last month we heard from Mr. Mead, the Inspector General. This subcommittee heard his testimony, and he clearly indicated that we cannot continue to cut the FAA's capital budget and transform the national airspace system for the 21st century.

Regarding the General Fund contribution, I strongly support the provisions that Congress enacted in Air 21, particularly the guaranteed funding provisions and the Trust Fund in general contribution formula. The FAA's programs should be fully funded at their authorized levels. If the Trust Fund revenues fall short, the General Fund should continue whatever it takes to meet the authorized levels.

Mr. Chairman, as you suggested in your opening statement, there are a number of alternative financing ideas that have been put on the table. One is the wholesale adoption of cost-based user fee. While I am open to all ideas, I think the idea of switching to a user fee system raises more questions than answers.

Additionally, some have suggested that Congress ought to consider alternative financing such as bonding. However, before Congress considers bonding authority, I believe the FAA should explain precisely what it would purchase with this authority, and how the authority will impact the Federal discretionary budget.

Mr. Chairman, these are important issues that we are dealing with today for the future of aviation, and I want to thank you again for calling this important hearing. I welcome our witnesses who will be testifying today, and I look forward to hearing their testimony.

Mr. MICA. I thank the gentleman. Mr. Coble?

Mr. COBLE. Mr. Chairman, I am plagued with an allergy, and I think my voice would sound annoying. So I will waive an opening statement.

Mr. MICA. Well, we will go to Ms. Kelly. I think she is in fine voice.

Ms. KELLY. Thank you, Mr. Chairman, and I want to thank all the witnesses. The aviation industry contributes $900 billion to the United States economy every year. The skies over the United States of America are the safest in the world, and I think it is crucial that we make the investment necessary to modernization and infrastructure improvements, so that the rates of returns and the success that we see now continue.

I am not sure that using the Trust Fund as the chief means of funding for operating expenses is the best way to make an investment; nor am I convinced that altering the collection of fees would not have a profound and detrimental impact on our General aviation system.

In her testimony, Administrator Blakey states that there is a need for an open dialogue in regard to the future of the Trust Fund. I could not agree more. I am delighted to see that statement there.

It is critical that all aspects of the aviation industry, from commercial airlines to General aviation, to the controllers who make our skies the safest in the world, have their voices heard on how the monies will be collected and how they will be spent.

With two years remaining before the current authorization expires, the decision of the Administrator and Secretary Mineta to listen to all the voices is a demonstration of sound judgment. I hope they do indeed keep an open ear.

It seems that passenger levels are returning to our pre-9/11 levels, and the projections are for over one billion passengers per year in the near future. So the decisions we make in the next couple of years are going to have a significant impact on our ability to handle the new strain on that system.

Right now, two thirds of the world's aviation dollars are spent right here in America. I would like to keep it that way. So I look forward to the testimony of all of our witnesses, and to hearing their answers on how we are going to solve today's problems, so we do not have them tomorrow.

Thank you, and I yield back the balance of my time.

Mr. MICA. I thank the gentlelady. Ms. Tauscher?

Mr. TAUSCHER. Thank you, Mr. Chairman, and thank you for allowing me to make this brief statement this morning.

As the Chairman has already described, the Aviation Trust Fund faces an unpredictable future. I look forward to today's conversation about the current state of the trust fund, and what I am sure will be a lively discussion of future reforms.

While most witnesses will discuss the financial health of the Trust Fund and their ideas for ensuring its ability to fund aviation needs into the future, I believe it is equally important to discuss additional steps that the FAA must take to determine cash flow expenditures and priorities for present and future capital expenditures.

Before Congress makes any changes that would alter the Aviation Trust Fund funding formula, we must require the FAA to continue to thoroughly examine how to control costs and make decisions on projects which have been delayed for years.

For example, for several years, I have questioned the FAA's procurement for modernization of terminal air traffic control facilities. The cost of the program adopted by the FAA has now, according to the DOT, reached over $2 billion, some $900 million over budget.

Beyond continuing to update program baselines for this project, the FAA must make realistic assessments about its commitment to programs with skyrocketing price tags. I believe that during his testimony today, the Inspector General will speak more to the need of the FAA to continue assessing its future requirements, before additional revenue streams are explored. I thank him in advance for bringing this important issue to the attention of the Subcommittee.

I would also like to thank Administrator Blakey for her willingness to continue to provide me and the Subcommittee with thor-

ough answers to our questions and for taking time to be with us this morning.

Mr. Chairman, I thank you for the time and I yield back.

Mr. MICA. I thank the gentlelady. I now recognize the pilot from North Carolina, Mr. Hayes.

Mr. HAYES. Thank you, Mr. Chairman, and thank you for holding the hearing today. It is vitally important that we maintain the balance with the system, as Mr. Costello, Ms. Kelly, and Ms. Tauscher and others have said. As we look at the Trust Fund today, I think it is very important that we do not get carried away with the idea of user fees. I do not see exactly how that is going to get us anywhere.

I appreciate all the participants being here today. The fuel tax and how that affects General aviation, and their ability to pay their fare share into the system seems to be the way to go.

The Energy Bill, with more reasonable costs of energy, with cooperation between the airlines, I think we can achieve what we do need to achieve and what we all are looking for. Again, I applaud the FAA air traffic control system, providing the kind of safety, efficiency, and consistency that we all have come to know and, hopefully, appreciate.

I look forward to hearing the panelists today. Again, let us make sure it stays fair and balanced. Thank you very much, Mr. Chairman, and I yield back.

Mr. MICA. I thank the gentleman. Ms. Norton?

Ms. NORTON. Thank you very much, Mr. Chairman, for helping us, I hope early, to face the dilemma that confronts us with the Aviation Trust Fund. When everyone deals with capital costs in the Federal sector, from the Federal Government, you have got to take yourself out of the real world and into the way we do it. The upfront funding of capital costs is done only here by the Federal Government.

I am on another committee, and I have to tell you that whereas nobody in the real world would do real estate that way, that is the way we do real estate in the District of Columbia. You have to authorize and appropriate the entire amount before you can put a shovel in the ground.

I agree that if there is barring from the Treasury to be used for capital costs, it obviously comes at a reduced cost. But I have to ask, compared to what? I do not know if bonding fits. Frankly, I am so distressed at the state of the Aviation Trust Fund, that I am open to any and all ideas.

But one idea is this. Obviously, it seems to me, it is one that would have to be off the table, given the pathetic, or should I say to be polite about it, terrible state of major airlines in our country.

I am very pleased to see that regional and large airline representatives are going to be here to testify, so that we get a more vivid picture. But the notion of increasing user fees, particularly at this moment in time, would seem to be unthinkable.

It is like what this Congress says it will not do most of the time, like increasing taxes. I just do not even see how that is a reasonable or practical alternative.

I do know this. If you were to think of the multiple ways in which you define what a great power is, one of the ways would be

to look at its airline industry. When you see where ours is, you recognize that the decline of our airline industry has an effect on the economy and on commerce in the United States, that a great power simply cannot afford.

I think that we need some action to clarify this matter in what I, Mr. Chairman, am the first to concede is a real dilemma. I think we ought to be open to practical action that strengthens the airline industry and strengths the Aviation Trust Fund. Thank you very much, Mr. Chairman.

Mr. MICA. I thank the gentlelady. Mr. Poe?

Mr. POE. I appreciate you holding this hearing today, and I want to thank the witnesses who are appearing.

The current statutory formula as expressed in the Aviation Investment Reform Act for the 21st Century requires that Trust Fund revenues first be used to fully fund the FAA's capital programs, such as the Airport Improvement Programs, facilities, and equipment, at the authorized levels; and also fund research and development before being used to fund FAA operations.

Mr. Chairman, I represent the Greater Houston Area. Houston is the fourth largest city in the United States; and our city's airport system has undertaken many major infrastructure improvements over the last few years at George Bush Intercontinental Airport and Hobby Airport, to meet dramatically increasing traffic demands. These include large capital investments, including new terminals, new runways, and other infrastructure improvements.

Airport improvements alone though cannot meet the projected demands placed on the aviation infrastructure unless the pace of the air traffic control modernization keeps up and the investments in these facilities can be effectively utilized.

The peak arrival rate at Intercontinental Airport is capped at 147 flights per hour, and that level is already being reached during peak operational periods. According to forecast, the peak arrival rate per hour will rise to 220 by 2020.

The Houston air traffic system was created in 2001 as a vehicle for funding a new Houston TRACON, terminal control facility, or FAA facility that controls arriving and departing aircraft and traffic in a 50 mile area.

Both the old facility and the equipment are in dire need of replacement in order to meet the increasing demand. The facility's age and location make it unreliable, due to the fact that it is below sea level and our last hurricane flooded the entire system.

It is also in a non-secure area, because it is close to a farm to market road. In addition to the looming congestion problem, inadequacies of the current TRACON facility forced the FAA to use inefficient sequencing of traffic arriving in and departing from Houston airports. Frankly, this has contributed significantly to neighborhood noise complaints.

Monday night, I had a townhall meeting for over 300 people, who were complaining about the FAA's inability and lack of moving forward with the TRACON facility because of the noise. Funding for the construction of a new TRACON facility has been approved and appropriated by Congress over the last two fiscal years, and the FAA has studied the issue for several years; yet, nothing has happened.

Even the City of Housing has allocated 100 acres of Texas land free, at no cost to the Government, for construction of this facility. However, the FAA is still not committed to beginning construction, and no one knows when this will happen.

I, as well as many other members on both sides of the aisle from the Houston area, believe strongly that this decision must be made. Given that the current arrival rates at this airport are at the maximum levels during peak periods, another further delay in beginning construction will make it impossible for the airport system to meet community air service growth needs, as well as responding to the growing noise concerns by the numerous area residents.

So briefly, I would like to know what the timetable is for the FAA's decision on building the new TRACON for Bush Intercontinental Airport. Thank you, Mr. Chairman.

Mr. MICA. I thank the gentleman. Ms. Boswell?

Mr. BOSWELL. Thank you, Mr. Chairman, I appreciate you having this very timely meeting. If we think of the precarious condition that we find out Nation's airline industry in, this is truly an important and timely hearing to examine the condition of the Aviation Trust Fund.

It is important for us to take a moment and determine where we have been, where we are, and where we are going with our aviation system. I, like many members of this Subcommittee, am a strong proponent of our Nation's aviation infrastructure. To maintain our first-rate system, adequate resources must be available.

Some have raised concerns about the future and how we can maintain FAA operations and capital investments with our present funding situation. The shrinking discretionary portion of the Federal budget raised great concern about our ability to maintain existing FAA operations and capital improvements.

There has been some discussion, but unfortunately it has been minimal, of raising user fees on aviation users, both on passenger and General aviation. In my opinion, this would be not only unwise, but harmful to our aviation system.

With our Nation's airlines already hemorrhaging red ink, any additional fees would certainly hasten their demise. As a strong proponent of General aviation, I am an aircraft owner and a pilot myself. I maintain our GA users already pay a fair share for the use of the system. I would strongly oppose any effort to change the fee structure already in place. Thank you, Mr. Chairman.

Mr. MICA. I thank the gentleman. Do any other members have opening statements?

[No response.]

Mr. MICA. If not, we will go right to our first panel of witnesses. We welcome back some repeat offenders here. We have the Honorable Marion Blake, Administrator of FAA; the Honorable Kenneth Mead, Inspector General, Department of Transportation; and Dr. Gerald Dillingham, with GAO. They have changed it to Government Accountability Office. I will never get used to that.

We welcome all three of you back, and we look forward to your testimony today. Let us hear first from Administrator Blakey; welcome, and you are recognized.

TESTIMONY OF THE HONORABLE MARIAN C. BLAKEY, ADMINISTRATOR, FEDERAL AVIATION ADMINISTRATION; THE HONORABLE KENNETH M. MEAD, INSPECTOR GENERAL, UNITED STATES DEPARTMENT OF TRANSPORTATION; DR. GERALD DILLINGHAM, DIRECTOR, PHYSICAL INFRASTRUCTURE ISSUES, UNITED STATES GOVERNMENT ACCOUNTABILITY OFFICE

Ms. BLAKEY. Thank you, Mr. Chairman, and I must tell you, I very much appreciate the opportunity that you and Congressman Costello have given us, and the members of the Subcommittee. Thank you for the opportunity to be here.

I am here today because we have a problem with the Aviation Trust Fund. As you know, the Trust Fund pays a large share of the bills for the FAA to operate the National Airspace System.

A troubling gap has begun to emerge between the revenue that comes in and what it costs to run the FAA. This has driven down the Trust Fund's uncommitted balance very sharply.

The taxes and fees that support the Trust Fund all expire in 2007. I would like to commend this Subcommittee for your foresight in recognizing the urgency of this matter.

The time we spend addressing these issue today will pay considerable dividends in the future. In fact, unfortunately, during the last reauthorization in the mid-1990s, the debate lasted nearly two years. The taxes and fees expired, and the aviation system lost about $5 billion which, of course, was never recovered.

This time, there is very little cushion. Because of today's higher revenue and appropriation levels, the expiration of taxes without replacement could be even more costly. So we cannot allow it to happen.

For this reason, last week Secretary Mineta and I convened a day and-a-half forum on the Trust Fund. More than 150 leaders from Government, industry, and Wall Street gathered to discuss the issues and make recommendations.

I brought along two charts to depict the problem at hand. As you can see in chart number one here to my left, today there is a significant gap between the revenue coming into the Trust Fund and the costs of what it takes to run the system.

There are three factors to consider. First, the excise taxes expire in 2007. Second, airline prices are dropping, and that is largely what fuels the Trust Fund. Number three, the shape of the industry itself is changing rapidly.

Despite our forecasts, we cannot be sure what the aviation industry will look like in the future, or the revenue it will generate. Because of a disconnect between the Trust Fund's revenue stream and our costs, the revenue generated for the Trust Fund is unlikely to cover the FAA's costs, particularly as they grow over time with the volume of traffic increasing in the system.

The second chart over here to my right shows that the uncommitted balance in the Trust Fund continues to drop. You would have to go all the way back to 1983 to find a lower balance in a year when taxing authority did not expire.

In prior years, relatively higher ticket prices helped keep the Trust Fund solvent, enabling the FAA to make investments for the future, while operating the world's safest transportation system.

But the chart points to an unfortunate and undeniable trend. This is not going to change any time soon. Low cost carriers are now the most significant driver of industry pricing. Because over half of the Trust Fund receipts come from a 7.5 percent excise tax on airline tickets, these lower fares decrease Trust Fund revenue without any corresponding reduction in FAA workload.

In addition, the airlines are taking many more deliveries of smaller aircraft. By 2008, we forecast that the United States regional jet fleet will be four times the size it was in 2000. Similarly, the United States business jet fleet will be approximately 50 percent larger than its 2000 levels. This means more aircraft, but decreased revenue per aircraft, using the air traffic control system.

There are also implications for our certification activities, as well. To date, there are 16 airlines waiting in the queue for certification. That is 16 new carriers, which will mean increased duties for our inspectors, who also have to oversee all those additional pilots, planes, and crew.

The increased workload is further compounded by a new generation of UAVs and micro-jets, and they are coming at us. This increased workload does not factor in the simple and direct costs of our safe, but aging, infrastructure, as a number of you have noted this morning. Estimated replacement costs of all of our assets right now is $32 billion. Of course, this does not address the looming need to move to the next generation system.

As this Committee well knows, we have made great strides in operating the FAA like a business, and conserving everywhere we know to. We have a new financial and cost accounting system, and I am very proud of the hard work and the success we have had at cutting costs. But I do not think we can get to be where we need to be, from the standpoint of this picture.

We are consolidating HR and accounting. We have increased our productivity. We dropped over 1,300 staff in the ATO last year alone. We contracted out the network of flight service stations, which were costing us approximately $500 million per year to operate. Unfortunately, those facilities had become very old, and the equipment was outdated. We will save the taxpayer $2.2 billion by that.

But cost cutting alone will not enable us to close the existing gap between the revenue stream into the Trust Fund and FAA costs. This presents a very unattractive list of options.

Do we cut services, such as air traffic control, certification, inspection? Instead of buying new equipment when we need to, do we just retain and try to maintain the aging infrastructure?

Now there are those who would still like to believe that the future of the Trust Fund is not in trouble; or at the very least, it is not as bad as it seems. They say our revenues will increase as passengers make their way through the turnstiles more than ever before, and somehow it is all going to be okay.

But unfortunately, the funding gap is very real. In our recent forecast, just as has been noted this morning, our forecasts have been too rosey. Given the deficit and other issues of national and international concern pulling at the General Fund, we cannot plan a greater share of the General Fund, a greater slice of that pie, is going solve our problems.

The reality is that the General Fund is tight, very tight. The Administration supports its use for part of the systems cost. But it just is not our answer to our long-term needs. We have to explore funding options that are in the long-term best interests of the aviation industry and the FAA.

As you are aware, just last December, Secretary Mineta launched the plan for America's next generation air transportation system; a system that Europe and others are already moving out smartly on. It aligns the revenues, resources, and plans of seven different Government groups.

But certainly, no one thinks that the Trust Fund, as it is constituted now, can pay to make the capital investments for the next generation system. So the fair question remains, how can we afford it? The answer, equally plain, is that we cannot afford not to.

In closing, I cannot overstate what has become all too clear. The FAA needs a consistent, stable revenue stream, one that is fair to all users of the system, and one that is not tied to the price of an airline ticket; a revenue stream that reflects our actual costs to provide the service.

Now look, at this point, I am not endorsing new taxes or user fees. But we must address the gap that exists between our costs and our revenues. It is the only way we will be able to operate and maintain the world's safest system with the capacity our economy needs. To be ready for tomorrow, we have got to start on this today. Thank you for doing so.

Mr. MICA. Thank you for your testimony. We heard some partial bad news, and now we will get the really bad news from Mr. Mead; welcome, go right ahead.

Mr. MEAD. I would just say, for Secretary Mineta, Administrator Blakey, and this Subcommittee, you are taking an important step by starting to address this issue now. It is a couple years in advance of the reauthorization. There are very contentious issues. It is good to start thinking about them.

I would like to speak first about the financial shape of the FAA. For as long as I have been associated with this issue, the big issue has focused on the increasing revenues in the Trust Fund, and why are they not being spent? The build up of big uncommitted balances was the focus of the debate.

That is no longer the case. Like the airlines, the FAA now faces a significantly changed landscape. Air traffic levels continue to show improvement, but expected Trust Fund revenues are not materializing.

FAA in 2001 estimated over $14 billion in 2005, but current projections indicate collections of about $11 billion. That is $3 billion less than FAA expected.

A chief reason for this, as has already been pointed out, is the 7.5 percent ticket tax yield, especially for business fares. A frame of reference, in March of 2000, the average cost of a ticket for a 1,000 mile flight was $150. In March of this year, the same ticket was about $118. So that is a pretty big drop.

A lot of people think that that is a permanent change. FAA's budget, meanwhile, is remaining relatively flat, about $14 billion. Within that amount, FAA's operations account, which is mostly staff, salaries, and so forth, has seen back-to-back increases.

At the same time, the airport account and the capital account, have seen reductions of a half billion hit each. As we testified last month, the current level of capital funding is not sustainable. Why is this? It is because long-delayed ACT projects have experienced so much cost growth of nearly $5 billion over original estimates, that there is little room for new initiatives.

Growth in the operations account, a high salary base, and the need to hire additional controllers to replace those that are retiring, are also major contributing factors.

So taken together, those factors explain why most of FAA's efforts now focus just on keeping the shop running. That is also why there is so much discussion about how to finance air traffic management initiatives.

I would like to speak to controlling costs and determining requirements. I see four pre-conditions for determining the extent of the financial shortfall and whether additional revenue streams are needed.

First, FAA needs to determine its current cash flow requirement for what is already on its plate, and make decisions on big modernization programs that have been long delayed like STARS.

Second, FAA needs to determine what the agency can do, in addition to what it is already doing, to control costs and curb waste and efficiencies. We outlined a number these things before the Subcommittee last month, Mr. Chairman. Among them was getting a firm control on huge indefinite quantity contracts, valued at over $2 billion, and taking proactive steps with the new $2 billion program that we have placed to replace computer and hardware platforms at en route centers. Actually, it is the computer brain that runs high altitude air traffic.

Regarding support contracts, we have got serious concerns over exactly how some contractor work is differing from the work that FAA employees do, but at much greater cost to the Government; sometimes double.

Third is getting FAA's cost accounting system in place and a labor distribution system. That is a must-have for anybody that wants to operate like a business. Taxpayers have already paid more than $50 million for this, and the system has been delayed for years.

But I am very pleased to report that FAA is making very real, significant progress here. This is a very meaningful change from the past, and it is a tribute to the commitment of Administrator Blakey and her team.

Fourth is determining the funding requirements for the next generation ATC system; what capabilities will be pursued, and when they can be brought in line. If more dollars are needed, the banker needs to be told how much, when, and for what. FAA expects to have this information later this year.

Let me talk about financial options for a moment. I think once the FAA takes these four steps, Congress and the Administration will be in a better position to judge exactly what the financial requirements are and explore options.

None of these options are painless. I will speak first to the General Fund. Over the past 10 years, the General Fund has provided, on average, about 21 percent of FAA's budget. General Fund con-

tributions for FAA's budgets have dropped sharply, however, from $3.2 billion in 2003, to $1.6 billion estimated for 2006. The general fund will represent 11 percent of FAA's FY 2006 budget. So that is a pretty big shift.

Given the competition for Federal funds from other Federal programs and the current Federal deficit, it is going to be a heavy lift to expect a General Fund increase beyond what has historically been provided.

I do think, though, that the debate on financing would be much better informed if the specific level of funding from the General Fund was identified for planning purposes.

Taxes, the ticket and the segment tax combined, make up about 70 percent of Trust Fund revenues. As was noted in the National Civil Aviation Review Commission Report in 1997, there has been controversy about the equity of the current system, and whether all users are paying their fair share.

Even if higher tax rates were a consideration, the airlines contend that they cannot pass on any tax increases to the flying public. I think Administrator Blakey has pointed out in her testimony quite well that the current tax structure really does not correlate well with the cost of providing air traffic services. And she is right.

User fees, this is not a new idea, either. Efforts to adopt user fees have met with stiff opposition from some quarters in the past. Today, we are facing the same debate, but the landscape is somewhat different.

First, FAA is facing a much bleaker revenue forecast. Second, they are much closer to having a cost accounting system in place than they were the last time this subject came up. But the contentious issues of who should pay what, and whether each stakeholder is paying their fair share remain unresolved issues.

In bonds and/or borrowing, I think this is a somewhat radioactive subject, but I might as well bring it up. Bonding and borrowing, this would allow FAA to sell bonds on the capital markets. This is not a new idea, either. It too was recommended in 1997 by National Civil Aviation Review Commission. The idea here is that bonding would give FAA the ability to raise large amounts of capital up front, and accelerate Air Traffic Modernization programs.

But granting FAA any type of borrowing authority is going to require legislation and consideration of complex budget scoring issues, as well as impacts on the Federal deficit.

There are two basic bonding models. The first does not impose any accountability, really, on the person borrowing the money. The second one does.

The first, we call the Amtrak model, because it was a proposal based several years ago in connection with Amtrak and inner city passenger rail. Under this construct, bonds would be sold to the capital markets, with a portion of the bond proceeds set aside to repay the principal for 25 years.

You put it in a bank account or a high interest-bearing bank account, and by the time the bond matures, you have enough money to pay back the face value. But rather than cash, investors would be given a tax credit, to provide the return which is guaranteed by the Government. A variant of this model is to pay cash and dedicate an existing tax for that purpose.

A serious problem with this construct, however, is that there is little or no incentive for improving accountability. The investment is essentially guaranteed. There are no incentives for cost control or delivering a project on a budget or on time. The idea here ought not to be just simply to give FAA more money, but to use funds wisely with a direct link to airspace users.

That brings me to the second construct for bonding. This is more akin to what happens in the private sector. Bonds would be issued in the public markets. This type of bonding scenario is almost a natural element of a financing system based on cost-based user fees. Because the fees would provide a bondable stream of revenues, they could be adjusted up or down.

There is also a built-in accountability factor here. Namely, there would be an oversight board that would set fees, not the FAA. This arrangement would provide powerful incentives from users to deter the cost growth and schedule slips that could be translated into higher fees.

Finally, there is peak hour pricing. This whole debate about FAA financing needs to be joined with the issue of peak hour pricing at airports such as La Guardia. It presents difficult policy issues.

First and foremost is whether Congress should allow peak hour pricing to begin with. If so, the questions become who sets the fees? Who gets the funds? Does the airport get them? Does the FAA get them, or does some combination of the two get them? What will the funds be used for and what would their impact be on service to smaller communities? Thank you, Mr. Chairman.

Mr. MICA. Thank you, and now we will hear from Dr. Dillingham with the GAO.

Mr. DILLINGHAM. Thank you, Mr. Chairman, Mr. Costello, and members of the Subcommittee. As most of you know, the Trust Fund was established in 1970 to help fund the development of a National Airport and Airway System. This graphic shows that the revenues for the Trust Fund are derived from a series of taxes paid by passengers and airlines.

The majority of those revenues come from the tax on airline tickets and the fee charged for each flight segment. When we look at the Trust Fund revenues over time, we see that revenues have fluctuated from year to year, but have generally trended upward.

This graphic shows that during 1981 and 1982, the amount of revenue coming into the Fund was about $500 million. This was lowest amount in the Fund's history, and was due in part to the lapsing of the aviation taxes.

The dip you see on the graph for 1996, again, reflects the lapsing of the aviation taxes. In 1999, you can see that the revenues flowing into the Trust Fund total about $11 billion, which was the largest amount in the Fund's history. After 1999, the amount of revenue started to trend downward.

There are several key factors that contributed to this decline in revenues. First was a dramatic drop in passenger boardings, that was exacerbated by 9/11 and the SARS outbreak. Another significant factor was the increased growth of low-cost carriers and fare reductions by the legacy carriers.

Now I would like to turn to how the Trust Fund revenues were expended. In this 2004 example of the Trust Fund expenditures,

operations accounted for 43 percent. AIP and F&E accounted for 29 and 27 percent, respectively.

This graph, which shows historical trends in Trust Fund revenues and expenditures, indicates that the amount of money flowing out of the Trust Fund to FAA's major accounts has generally increased each year; and that between 2002 and 2004, expenditures exceeded revenues.

This graph shows that the principle reasons for the increase in Trust Fund expenditures are the increases in AIP grants shown in blue, and the increases in the amount of FAA operations that were funded by the Trust Fund that are shown in red. AIP has increased from about $1.5 billion, in 1998, to $3.5 billion today.

This graph shows the operations budget over time, with the Trust Fund contributions shown in red, and the General Fund contributions shown in blue. It shows that from the time the Trust Fund was established, it has paid some portion of FAA's operations.

It also shows that in 1972 and in 2000, the Fund provided 100 percent of the cost of operations, and is expected to cover about 63 percent in 2005.

As a result of the changes in revenues and expenditures, this graph shows that the size of the Fund's uncommitted balance has started to decrease substantially. It shows that the uncommitted balance decreased from $7.3 billion in 2001, to $4.8 billion in 2002, and has continued to decrease by about $1 billion each year since.

Now I want to focused on the aspects of our work that focus on the projected outlook of the Trust Fund from 2006 and beyond. We examined the possible outcome of the Trust Fund under Vision 100 authorization and the President's 2006 budget proposal. Our preliminary findings indicate that the Trust Fund will have sufficient revenue to fund authorized spending and end each year with an uncommitted balance through 2007.

This is true both under Vision 100's scenario shown in blue, and the President's 2006 budget proposal, which is shown in yellow. It is important to note that these Trust Fund projections are very much dependent upon achieving forecasted traffic levels and air fares.

As you can see in this next graph, during four out of the last five years, FAA has over estimated the revenues going into the Trust Fund. During 2003 and 2004, the actual revenues fell short of forecasted revenues by almost $1 billion each year.

To take this circumstance into account, we also conducted a sensitivity analysis, wherein we examined the future of the Trust Fund under alternative scenarios. For this analysis, we assumed five and ten percent less tax revenues going into the Fund.

The preliminary results of that analysis shows that if revenues were five percent lower than the projected level, the Trust Fund's uncommitted balance would fall to less than $1.5 billion, under both the President's proposal and Vision 100, in 2006 and 2007. If revenues were 10 percent lower than the projected level, the Fund's uncommitted balance would reach zero in 2006, under the President's proposal; and in 2007, under Vision 100.

The question that remains is, how do projected revenues beyond 2007, compare with projected costs for development, operation, and

maintenance of the Nation's ATC system. FAA projects a five year cumulative $8.2 billion shortfall for the ATO; $5 billion for the operations account; and $3.2 billion for the capital account.

If this is accurate or even close to accurate, it presents a tremendous challenge for FAA and the Congress. Congress and FAA will have to address not only the revenue side, but also the cost sides of the ledger.

On the revenue side, there are several options being discussed, as we discussed this morning, that range from a version of the status quo with excise taxes, to some form of bonding, to a cost-based user fee system. We are currently examining some of these options in our ongoing work for this Committee.

On the cost side, the cost control initiatives that FAA has thus far identified do not even begin to close the $8.2 billion gap.

We believe that a critical first step should be the development of a strategic business plan for ATC modernization, that would also include initiatives that focus on big ticket cost savings, such as the greater use of CTI graduates to fill the controller ranks, elimination of redundant ground-based NAV aids, and facility consolidation.

Mr. Chairman, in the final analysis, we believe that the discussion about how to finance FAA and its operations beyond 2007 must not only focus on how to provide more money, but also on cost control improving the management of its operations. Thank you, Mr. Chairman.

Mr. MICA. Thank you, and I thank all of our witnesses for their testimony. We will start with some questions, and I have a couple to begin with.

First of all, Mr. Mead, in reviewing who pays what, as far as funds into the Trust Fund and paying for FAA services, I think you testified that the General Fund is paid, on average, 21 percent. I look at that as being fairly consistent.

When you look at General aviation and commercial aviation, and maybe the military or others, what users are paying their fare share, in your estimation, and who should be paying more or less?

Mr. MEAD. Well, that is a tough question to answer, determining if users are paying their fair share. I can tell you that commercial aviation accounts for approximately 65 to 67 percent of flight activity. They are paying a little over 90 percent of the revenues coming into the Trust Fund, through various taxes. There is the ticket tax. There is another one called the rural airport tax. There is another one called the way-build tax.

There is also a commercial jet fuel tax, international departure/arrivals tax and a frequent flyer tax. When you add these taxes up, it is a little over 90 percent.

Mr. MICA. So commercial aviation is paying a fair share, you believe?

Mr. MEAD. I think they are.

Mr. MICA. So we do not need Mr. May to testify later?

Mr. MEAD. No, I think he can discuss these issues much more eloquently than I can.

Mr. MICA. Okay, let us get into General aviation.

Mr. MEAD. There are a number of issues about General aviation. Basically, General aviation and jet fuel is generating about 1.92

percent of the Trust Fund Revenues. That is on the fuel tax, which yields about $178 million.

But there are a lot of questions as to whether or not some portion of the General aviation business share is actually being counted by the IRS as part of other taxes.

Why is that? Well, for example, with commercial jet fuel tax, some of those taxes are actually being paid by users that would qualify as General aviation. But in actuality, the Internal Revenue Service, the way they count it, does not stratify it between the regular commercial airlines and General aviation. So there is some question there.

Secondly, the United States aviation system was basically set up for the airlines. It was not set up for the general aviators, and the General aviation people state they are incremental users of the system.

Mr. MICA. Well, as to use of the system and cost and contribution, you are still saying commercial aviation pays it share and more, in your estimation.

Mr. MEAD. Yes.

Mr. MICA. General aviation probably has many more planes in the sky and is paying a smaller share. Is that a general conclusion?

Mr. MEAD. Yes, I think that is arithmetically obvious. We did an analysis of operations at the en route centers, control towers, and of IFR operations. We tried to back out of that, as much as we could, the non-business General aviation user.

What you end up with is, in the en route center, 57 percent of operations, were commercial carriers. The commuter air taxis were another 21 percent. General aviation, and this would mostly be business use, was about 18 percent. The military was a smaller figure and has to be handled quite differently.

When we reviewed control tower operations, about 20 percent were air carrier, 27 percent were commuter air taxis, and 42 percent were General aviation.

Mr. MICA. When you say air taxi, what is your definition?

Mr. MEAD. Well, commuters air taxis, I meant for hire.

Mr. MICA. That would also include your business jets?

Mr. MEAD. No, that would not.

Mr. MICA. All right, I am trying to get some idea on who is using the system and who is paying into the system. I have a quick question for Administrator Blakey. For costs, one of your biggest costs is labor. I think you had an agreement back in 1998, and I think you expected some costs in 1998 as far as labor.

As the air traffic control force, what has been your actual experience and cost to the system, as opposed to what was anticipated, based on your original projections?

Ms. BLAKEY. The original projection of cost increase of that initial contract, over three years, it was expected to increase costs by about $200 million. The actual costs were a $1.1 billion increase. So it was very significantly under-estimated, in terms of what the cost of the controller contract would be.

Over time, we have seen controller compensation go up 70 percent. So there is no question about the fact that it is a significant part of the aviation systems operation costs.

Mr. MICA. I will sort of conclude here because I want other members to speak, but I have a number of questions. One of the things that we have seen as testimony today is that the current core revenue stream is based on basically passenger ticket taxes and percentages.

We have also seen sort of the beginning of a discount industry. I predicted that we would see even more discount carriers, and probably lower prices. Actually, I think it has taken place much more rapidly than I anticipated.

This is a list that I had the staff print out of European discount carriers. This is about eight pages of European discount carriers, and I think we are headed probably to see commercial passenger service even more on a discounted basis than the traditional legacy carriers. I think everybody agrees that that is going to also drop our revenues and create more of a problem, Ms. Blakey.

You said, and I took this down, you are "not endorsing taxes or user fees," but you said the "ticket tax does not work."

Ms. BLAKEY. The ticket tax is absolutely unrelated to the costs of the service. There may have been a time when there was a somewhat closer alignment, but it might as well be pegged to the price of milk these days.

As we noted, there is the fall in yield, the fall in ticket prices, and the move to a much smaller aircraft. The front page of the New York Times this morning was noting that the major carriers are moving much more to point to point flying, to smaller cities. That all goes to smaller size aircraft, but it costs us the same amount to move that aircraft, regardless of whether it has got 50 people on board or 200.

So all of those are the trends, and as I mentioned, we have got 16 applicants for airline certification in the queue right now. I would suspect a lot of those are low cost carriers who want to get into the business.

Mr. MICA. That is not to mention the micro-jets and other increases in air tax-type services.

Ms. BLAKEY. The first of the very small micro-jets are expected to be certified next year, and the production delivery schedules are literally thousands a year.

Mr. MICA. Well, I will turn to Mr. Mead, quickly, and Mr. Dillingham, if you want to comment, and then I need to go to other members.

Mr. MEAD. I think it is an important point that, in today's environment, you have the legacy carriers and the discount carriers. The legacy carriers' fares for the foreseeable future, are going to be very competitive and may trend downward. There are going to be conversions. If you apply that 7.5 percent against a lower based ticket price, the arithmetic is pretty simple.

Secondly, there really is not a correlation between a fully loaded plane of one type, whose fares are cheaper, and a fully loaded plane of the same type. Yet, the costs they impose on the air traffic control system are fundamentally the same.

Mr. DILLINGHAM. Yes, we agree that what we are seeing now is that cost and revenue are, in fact, diverging. However, we just want to reiterate that with all the discussion about bringing in new

sources of revenues, that the other side has to be looked at, too, and that significant cost savings have to be a part of this mix.

Mr. MICA. Thank you, I have more question, but Mr. Holden is waiting.

Mr. HOLDEN. Thank you, Mr. Chairman, and thank you for holding this hearing today. I thank the panel for their testimony.

As you highlighted, we are facing challenges in the near future here as we try to balance our cost savings versus cuts in services and, of course, maintaining our attention towards safety.

Administrator Blakey, I would just like to follow-up on one of the proposals that I had a chance to talk to Mr. Chu about a few weeks ago when he testified here, about the proposal to close the air traffic towers at 42 airports across the country.

Mr. Chu told me that it was in the infancy of the study, and it was going to be progressing over the next 30 to 45 days. I am just curious if you can tell me where that study is at right now.

Ms. BLAKEY. Certainly. We are doing very careful analysis of the specific circumstances of all of those 42 airports.

I would stress that this is a process that the FAA has undertaken for years and years. It is done on an annual basis. It is an attempt to keep our costs in line with service. So when traffic figures drop in certain towers, it only makes sense to not staff those towers during the midnight shift, if there is no one flying in, or virtually no one.

So that is really at the hub of this. We did not do it for a number of years. Because we thought that traffic coming back after 9/11 would change things, and we wanted to give everyone a breather.

We will get that analysis done, I would suggest to you, within the next 30 days. I think his estimate was probably about right. We will certainly be consulting with any members whose towers are affected.

Mr. HOLDEN. I appreciate that, Administrator. I believe Mr. Chu said that the savings would be about one tenth of one percent of the entire budget. So I think he might have used the figure of $5 million or $4 million.

Ms. BLAKEY. That is probably right. What I would caution though about this is that you understand the FAA's circumstances are such that to ignore millions of dollars of savings is not something we can afford to do. This Committee and others are urging us to look everywhere we can for cost savings. A number of the suggestions that have been made this morning, frankly, would save less than that.

So it is something that I have to do, to look everywhere we can for incremental savings. This review has been something that has been standard for the FAA for many, many years.

Mr. HOLDEN. I understand that and appreciate that, and I realize you are going to hear 42 different stories. But I would just like to give you one of those 42.

Harrisburg International Airport is responsible for the airspace at two nuclear power plants, Three Mile Island and Peach Bottom, as well as being a major diversion airport for Philadelphia, Dulles, and Reagan. So I understand and appreciate that you will be in consultation with me as it progresses. But I know they will take all those factors into consideration.

Ms. BLAKEY. We will, and I also will point out that when towers have their traffic increase, then we also move back to staff them. So there is flexibility in this.

Mr. HOLDEN. Thank you, I yield back, Mr. Chairman.

Mr. MICA. Mr. Hayes?

Mr. HAYES. Thank you, Mr. Chairman. I feel like I need to clarify just a little bit. Mr. Mead had a good answer and the Chairman asked a good question. I think we need to focus on the fact that every time the airline cranks up, they use the system. That is fine. They should, because that is what they are there for.

There are thousands, I think, of General aviation airplanes, who never use any part of the system whatsoever, except the air, which is still free. But every time they buy a gallon of gas, they do pay into the system. So just to clarify, it was a good answer, but we just did not get all the details in there.

Administrator Blakey, again, thanks for your wonderful service. Certification offices have recently been informing our largest repair station facilities that approvals on projects will slow dramatically because of budgetary constraints. This has caused great concern among key members of the community. They have put millions of dollars into these projects, only to find out that approval may take weeks and even months before taking place.

Is the staffing situation at the FAA bringing aircraft certification approvals on million dollars projects to a halt, or have we got that under control?

Ms. BLAKEY. Well, certainly, we do not plan to bring any projects that we can foresee, Congressman Hayes, to a halt. The question is, how slow is the queue? How long will you have to be in the line?

I think that probably everyone on this Committee would agree that when it is a choice between new projects and overseeing the ongoing safety of the system, of the carriers of the existing facilities, the latteer has to be the first priority. We have to maintain safety first then proceed, as new facilities and new products want certification. We are doing the best we can to cover that.

I would point out that we are projecting right now that we will be down 300 people in our AVS area, which is where certification is. I would also point out that a lot of this is a result of the unfunded pay increases, and the recision. These are things that I realize this Committee is not responsible for. But those are the effects it does have. So we are doing the best we know how to, to meet those new requests, but they are new.

Mr. HOLDEN. I appreciate that comment. I think it is important that what you have also said there is that we have a responsibility to make sure that through the Appropriations process you have the funds that you need.

I have one more editorial comment, if I may. You talk about thousands of very light jets. If we do not get the insurance industry on board, there is not going to be anybody that can get insurance fly the darn things. So thank you again, and I yield back.

Mr. MEAD. Mr. Chairman, may I follow up on a point that Congressman Hayes was inquiring about, the 300 people that Ms. Blakey was referring to.

I think you should be aware that a lot of attention is focusing on hiring a significant number of controllers to replace those that

are going to retire. This is a legitimate concern because these retirements are going to occur and FAA has planned for this.

But at the same time, the safety inspection work force is going to lose 300 people. The FY 2006 budget does not propose to replace these people. Frankly, I have some concerns about that.

Mr. HAYES. That is a good point to keep in front of us. All of the members of committee are vitally concerned with safety first. We would be more than happy to work on behalf of safety as it relates to the overall air space and the FAA. Thank you, Mr. Chairman.

Mr. MICA. Ms. Norton?

Ms. NORTON. Thank you, Mr. Chairman. For this panel, I really have a question going to the possible long-term changes in the airline industry and how we can confront that at the same time as we confront the Trust Fund.

My question is really based on the correlation your testimony has shown between the Trust Fund and economic conditions in the airline industry. In fact, if we look at this industry over time, we see an industry that is almost cyclical. It is a roller coaster industry that is historically based on economic conditions in the country. When things got better, people began to travel more. Things improved in the industry.

We recognize there are lots of reasons that people do not have to travel as much any more. Among them, of course, are vast changes that are like an earthquake under us, because the occur every day in technology.

My question really goes to the extent to which you believe what we are seeing in the airline industry is truly structural. That is to say, everybody knows that there is downsizing. We see every line looking like a discount airline. That certainly tells us something.

Are we seeing structural changes in the airline industry today? If so, when will this stabilize? Is this going to stabilize soon? I cannot imagine that the industry is going to go down to nothing. At some point, when excess carriers are weeded out; at some point when you have discounted as much as you can discount to be competitive, surely this would stop. That may be at some low level that none of us want to contemplate it.

But I want to ask you, are we seeing something structurally different from the up and down of the airline industry, and is there any sense of long-term projections recognizing, of course, how completely unpredictable and untrustful such long-term projections often are; but given the nature of this industry, somebody, it seems to me, must be studying whether something very different is happening to this industry, and if so, what the nature of that change is.

Ms. BLAKEY. Everything we see, from the standpoint of our economic work in forecasting, says that there are very fundamental changes in the industry, and that it will not go back to the good old days.

Ms. NORTON. Well, I know that. The question is, what is it going to go back to?

Ms. BLAKEY. I think, appropriately, of course, our concern is really this dramatic change in the fleet mix and dramatic change in traffic, et cetera. But the Inspector General has done studies on this.

Mr. MEAD. Thanks, that was nice.

[Laughter.]

Mr. MEAD. The legacy carriers, including U.S. Air, Northwest Airlines, UAL, and Delta, are still trying to get their costs down. They are still not turning a profit. It is going to be awhile before they get their costs down.

However as they get their costs though and lower their fares, they are going to become very similar in cost structure to the discount carriers.

When that happens, I think there is going to be a powerful dynamic unleashed in the industry. The network carriers have the power of a network. The low cost carriers do not have as many hubs.

I know a lot of people think that what we are seeing is a permanent structural change. But I think once the cost structures are more aligned, you may see fares start to creep back up again.

Right now, one of the big phenomenon is the very sharp reductions in business fares. We have seen this consistently since 2001. But I think there may come a time, four or five years from now, when we see the cost structures of the big carriers more aligned with those of the low cost carriers. Then you will see some changes in the fares. There will be upward movement in those fares.

Ms. NORTON. Of course, that would mean other kinds of changes, as well, in traditional carriers.

Mr. MEAD. Also, I think you are going to see, as Administrator Blakey pointed out, a lot more point-to-point service. But hubs are probably here to stay.

Ms. NORTON. Finally, just let me say, I do not know how the changes in technology factor into this, and whether business travel will continue to be what is has been in the past. But if these changes are structural, and what you have just said says to me, you know, most airlines are going to be low cost airlines, I regard that as a structural change.

If these changes are structural, then it does seem to me that we have to confront the possibility that we will need structural changes in the Trust Fund, as well. Thank you very much, Mr. Chairman.

Mr. MICA. Mr. Graves?

Mr. GRAVES. Thank you, Mr. Chairman. I want to go back to what was pointed out, and Congressman Hayes briefly touched on it, on the number of GA aircraft that are out there. This is obviously being looked at as the great pot that we are going to pull money from to pay for the system, to an extent.

I keep hearing it in the industry. I hear the rumors talked about. I hear the talk of charging any flight service used, whether it is weather or whatever the case may be, or even takeoffs and landings. I do not know what is being looked at.

But I do know that we seem to be looking at that area. Congressman Hayes pointed out, too, that the vast majority of those GA aircraft are not using the system, to be quite honest with you. I mean, they are flying underneath the controlled airspace when they are going into a congested area. They are just doing VFR stuff.

They are not necessarily filing flight plans. They are not checking the weather. They are very low cost users of the air. I am curi-

ous, do you have any idea what the percentage of GA is out there that are using the system; any one of you?

Ms. BLAKEY. Congressman Hayes, we have done certainly some studies on that. If you are talking about the folks who are just flying VFR without using the system, those are not as directly tracked as they are, of course, if they are filing flight plans and flying IFR, et cetera.

What I can assure you is this. We are doing a cost allocation study. Because we really do believe it is important to look very carefully at those things, and look at issues of equity across the system.

So we are going to be analyzing the fleet mix. We are going to be analyzing a variety of factors to really understand what the costs are that are imposed all up and down the system. Of course, GA is comprised of a wide variety of users, as well.

So the person who uses the system for personal travel, if you will, for individual weekend recreation, is very different obviously than those that are using it for business purposes with very high performance aircraft. So all of that needs to be updated and analyzed, and I will assure you, we will do that.

Mr. MEAD. I think the biggest service that could be done in response to your question is to take the General aviation chunk, which is fairly large, and break it into pieces. There are groups who are very casual users of the system. They are not doing IFR approaches. They are not using air traffic control. Then there are higher end users. I do not think the two ought to be lumped together for purposes of analyzing the issues you are raising.

Mr. GRAVES. But they are being lumped together, unfortunately, in talking about, you know, where we can go to find some more money and in user fees.

In fact, it seems to me that if you do start taxing the use of flight service, if you start taxing on calling in to get a weather report, or takeoffs and landings, that is going to create a safety problem, in and of itself. Because a lot of those casual pilots are going to forego that weather report, or they are going to, if the weather is marginal, a lot of times they do not use weather anyway but they will call in if the weather is marginal, well, they may forget that. Or even practicing their landings, take-offs and landings, if you are doing some sort of a user fee on take-offs and landings, well, it is cheaper just not to do them. And then you get into a safety situation. It would seem that it is completely the wrong direction to go.

I think the perfect user fee is the fuel tax system that we have now. If you are flying, you are burning fuel, and you are obviously paying into the system. In fact, it can be argued that GA is paying, for what they are getting, is paying a lot into the system because they are burning fuel. But it disturbs me considerably this talk about going to user fees for general aviation, because I would say the vast majority of GA out there is those folks who are not taxing the system, who are not using the system a whole lot. It really concerns me.

I do have a historical question I want to ask. It seems to me when we first came up with the Trust Fund we were trying to get GA off the big airports. We wanted to come up with a secondary airport system to relieve our airports, I think was the actual term.

In fact, I remember looking at an article or a picture back in the 1970s of I think it was a TWA 747 on hold because it seems like it was a twin Barren was landing, and that was the problem with the system. So we created this Trust Fund to build infrastructure, to improve infrastructure which was off of the major hub airports and get GA out of the way.

We seem to be moving away from what the original intent was, which was infrastructure, and obviously moving to a point where it is paying more and more of what you all are doing. It seems to me like we have got to get back on track on where it needs to be and use the Trust Fund for what it was originally intended to be used for.

Ms. BLAKEY. One thing I think is important to understand, Congressman Graves, because I do appreciate the need to make certain that there are airports that the general aviation community can use, there has been a dramatic increase in AIP funding over the last four or five years. When you look at the increase in funding, it is very significant, a bit over a billion to last year it was $3.5 billion. This year in the fiscal year 2006 budget, we are still proposing $3 billion, and a very, very significant amount of that goes to small airports. So it really is important to understand how much that has really changed the landscape from that standpoint.

The other thing I would say is this. We are certainly very sensitive to the issue of safety. And the idea of avoiding important safety benefits in the system is something that we are going to be very careful about. It is important though to note that, just as an example, the figures that I have heard AOPA use about the fuel tax, for example, when we were discussing the issue of flight service stations, the GA community contributes about $60 million in terms of the fuel tax. The cost of flight service stations as they have been set up to this point was well over $500 million, and they are, of course, for the general aviation community. And even as we are driving the cost of flight service stations down—as you know, of course, we are moving with Lockheed-Martin who going to be providing that service at considerably less cost—the two simply do not match up. So there are certainly issues here that I think we all just need to be aware of.

But we are going to be looking for the best possible way of aligning the cost of the system for everyone in a equitable way, in the simplest possible way as well. So that is one reason why I do not think we should rush to judgment about user fees or excise taxes or any particular structure yet.

Mr. MEAD. You are correct in saying that the original design of the Aviation Trust Fund was for air traffic control and airport infrastructure. The operations in the original design would be handled through the General Fund. This is why it is so important for the Committee to get a handle on what the assumed level of General Fund contribution should be for the next reauthorization period. You are dealing with swings of $2 or $3 billion. That is quite a bit of money.

Mr. GRAVES. In closing real quick, I am glad you are not set, and I would implore you, I think user fees are the wrong way to go. We need to work together to figure out a way to do this. I would like to get us back on track and moving more towards GR for oper-

ations, figure out how we can do that, but we can come up with something. User fees are not the way to go, I do not think. Thank you, Mr. Chairman.

Mr. KUHL. Mr. Boswell?

Mr. BOSWELL. Thank you, Mr. Chairman. I would like to associate myself with the remarks that my colleague, Mr. Graves, made. Administrator Blakey, you recommended the FAA take some steps to control cost and determine the future requirements before they explore new revenues, and I appreciate that, including making decisions on necessary ATC modernization projects. What progress are you making? Can you give us a little update?

Ms. BLAKEY. We have been making I think really quite remarkable progress in terms of cost-savings. Some of the figures that are used about the overruns in cost, when you look at those and the facts on the major capital investment programs, usually go back to baselines in the 1980s. When you look at what we have been doing of late, we are doing a very strong job in making sure that our major acquisitions projects are coming in on schedule and on budget. Last year more than 80 percent were within 10 percent, which, considering again how much work we had to do on this, is really a very strong track record. Major projects like ERAM, for example, which is the central system for the Air Traffic Control system, is on time and on budget. So I would point those things out.

There are a number of other cost-savings that we are working very hard on in terms of things that we know can help control our costs. The very ideas that the General Accounting Office has recommended, that Dr. Dillingham has suggested, we are moving on all of those. I think it is important to note, though, that some of these are very hard to do if you want to have significant cost-savings. Facility consolidations mean, obviously, that choices are made that sometime can be very politically difficult to do. So I would simply call the Committee's attention to the fact that this is not all within the control of the FAA.

I would be happy though to enumerate a number of other cost-savings, if it would be helpful. I have got a whole sheet here.

Mr. BOSWELL. You might just cover a couple.

Ms. BLAKEY. All right. I would be happy to. Essentially, we have made a part of the FAA's business plan and our flight plan the requirement that there has to be cost reduction activities in every single one of our lines of business. Of course I noted the A-76 process, which is saving the taxpayers $2.2 billion in terms of the move to have Lockheed-Martin provide the flight service station function for us. We are consolidating accounting personnel, and implementing a centrally managed cost control program that we are putting in place this year for a variety of costs that the FAA has from the standpoint of IT and administrative costs. We also, of course, have a very strong contract tower program, which again is a cost-saving function there.

I could also tick down things such as consolidating our regional service units within the ATO, reducing management layers from 11 to 6, shifting the control of traffic in terms of these midnight shifts where we do not have a cost justification for staffing in towers where there really is no activity going on, and removing Navaids, nondirectional beacons. This is a question of aging infrastructure

out there that really is not contributing, from a cost-benefit standpoint, to the system. So I think that when you begin to look at a variety of things like that, there is no question about the fact that we will be saving costs, as well as in things such as reducing the time it takes to train our controllers. That is a part of the plan that we put forward to Congress in December. We are very optimistic about making real progress with that.

Mr. BOSWELL. Thank you very much. I suspect that Mr. Phil Boyer will have some information on Mr. Graves' questions that were asked earlier about a number of VFR activities going on that is not in use in all these things. Thank you, Mr. Chairman. I appreciate it.

Mr. MICA. [Presiding] Mr. Poe?

Mr. POE. Thank you, Mr. Chairman. In my opening statement I asked a question about the Houston TRACON. Also, just for your information, Congressman Culberson and McCall, also in the area, the three of us have written a letter asking when this is going to be built, at least started. I just want some assurance that within the next 30 days or so we get an answer. Okay?

Ms. BLAKEY. I will be happy to get back to you with the real timetable on that. It is obviously a very important facility and we appreciate that.

Mr. POE. Okay. The second thing was we have heard a lot of comments about money, which is really I guess the root of all things, evil and otherwise. Continental is the hub, Intercontinental Airport in Houston, and Southwest has a tremendous facility at the Hobby Airport on the other side of town. Airline consumers are paying 26 percent of a ticket price is taxes that goes to different projects, and the airlines are paying about 35 percent income tax plus fuel taxes, which is understandable why they are in trouble. Of course my concern, as everybody's is, is we want to keep them flying. We do not want them going broke and then somebody having to bail them out, which is usually the taxpayer.

It is an interesting phenomenon it seems that raising ticket prices does not work because the consumer finds a different alternative to flying. The best example is Continental flies Houston-Dallas, Houston-San Antonio, Houston-Austin, very close, and it reaches a market price where the consumer says I am not going to fly, I will just get in my old pickup truck and drive. And then the airline industry hurts when the price goes up for those little short hauls. Maybe that phenomenon does not work in other businesses, but it does work in the airline industry. So raising prices to cover taxes may not be the answer.

So I hope we can find an answer to the problem. We look to you to give us some concrete, definite answers to keep our airlines flying, safety is important as well. I appreciate your being here and I just wanted to make those comments about the TRACON and especially our airlines. So, thank you, all of you.

Mr. MICA. Thank you. Ms. Berkley?

Ms. BERKLEY. Thank you very much, Mr. Chairman. I want to thank all of your for giving us your testimony. I appreciate it very much. It was sobering, to say the least, and I recognize the challenges that we have. I am not sure that it is your responsibility to come up with the solutions. But perhaps together we can come up

with a way to keep airline prices down, not put all of the rest of our airlines in bankruptcy, and be able to provide safety for our flying public.

Last month, McCarren Airport, which is the airport in the Las Vegas area, had its busiest month on record, with 3.9 million passengers. Local officials, as you know, are moving forward with plans to accommodate the growth in the number of passengers, increasing the number of gates, and the county is also working on its plan to build the Ivan Paugh Airport that was passed a couple of sessions ago. It is my hope that the FAA will work with Randy Walker and our local officials to meet the tremendous needs of Southern Nevada. We just had another mega hotel come on line last week with over 3,000 rooms. We have 9,000 other rooms in some stage of development. For each one of those rooms, we are going to have thousands and thousands of people pouring into the Las Vegas valley and most of them are coming through McCarren Airport. So your help with that, as always, is greatly appreciated.

Ms. Blakey, I really want to thank you for your help in moving forward with the new Air Traffic Control tower at McCarren, and the improved runway conditions in North Las Vegas Airport which were a very serious problem for us. I do have a question for you regarding Air Traffic Control operations. I was sitting in this very seat and you were sitting there when we were discussing privatization and the contracting out of 71 FAA air traffic control towers. That was a subject of considerable debate in the 2003 reauthorization bill. One of those towers, North Las Vegas, is in my district. The one year moratorium on contracting expired last October. Does the Agency have any plans on contracting out the FAA air traffic control facilities as part of this cost-saving opportunity?

Ms. BLAKEY. There are no current plans in terms of converting air traffic control towers currently at this point. I think it is fair to say that if the FAA is urged by this Committee and everyone else to look for ways to save costs, it is important to take into account where we can do so. The fact is, of course, when you are looking at comparable facilities, a comparable contract tower versus a federally staffed tower saves $900,000 a year. So it is worth understanding that. But I have no plans at the moment.

Ms. BERKLEY. Well thank you for that. But let me ask you a question. When we say that it saves $900,000 for the FAA, but somehow, someway, someone is going to pay for that service. So for the flying public, do they not ultimately get the cost of privatizing the air traffic control system passed on to them?

Ms. BLAKEY. No, not at all. They get the exact same service whether a Federal controller is speaking to the pilot or a controller that is hired through a contractor. There is no difference, nor is there any difference in the cost.

Ms. BERKLEY. How do we pay for that service? Who ultimately pays the salaries of the air traffic controllers that are working for a private company as opposed to the FAA?

Ms. BLAKEY. They are paid through the FAA. In other words, the FAA pays.

Ms. BERKLEY. Then how do we save $900,000?

Ms. BLAKEY. Because, significantly, the salaries are much less in a contract facility than they are in a federally-staffed facility. They

also handle staffing differently than we do. And most of these, of course, are lower activity towers, VFR, et cetera, so in some cases, of course, there are differences in complexity as well.

Ms. BERKLEY. I would be very concerned if somebody that is a professional and can command a certain salary level would be so willing to work for a company and get so much less for their services. It seems to me that the FAA does a very good job, and the Government has a responsibility to provide the flying public with assurances that the air traffic controllers in this country are the best that they can possibly be. And I feel more comfortable myself knowing that the air traffic control system is under the FAA and Federal auspices.

Ms. BLAKEY. Both are under the FAA. Both are overseen by the FAA. Both forms of towers operate to the exact same requirements and standards and are audited. Candidly, the safety record of the contract towers is certainly as good as those of Federal towers. So there is no difference in either safety or service at all.

Ms. BERKLEY. Well, do not think we need to debate. We could debate this in private. But then why do they accept so much less pay?

Ms. BLAKEY. The salaries are fair salaries that are offered by the contractors. They often hire former FAA controllers, they hire former military controllers, and they have competitive salaries. The FAA salary structure for Federal controllers is very high. The average FAA Federal controller makes over $150,000 a year with salary and benefits.

Ms. BERKLEY. Okay. With all candor, I think they are worth every penny of that. And when I am flying every week, I like to know that we have got the best possible air traffic controllers in those towers. Thank you very much. I appreciate your help in Las Vegas more than you will ever know. Thanks a lot.

Mr. MICA. I thank the gentlelady. Mr. Duncan?

Mr. DUNCAN. Thank you, Mr. Chairman, and thank you for calling this very important hearing. I am sorry that appointments and then a hearing in another subcommittee which affected a plant employing several hundred people in my district has caused me to have to be in and out of this. And I have got to speak at a luncheon at noon, so, unfortunately, I am not going to be able to stay for all of the next panel.

I guess I only what to ask this or say this. We have heard a lot of testimony here this morning and we will hear some more from the next panel about the problem. But what we need is more testimony about the solution. Administrator Blakey, I did hear your testimony and you mentioned that meeting that you called with was it 150 leaders from the industry and all the parties affected. I am wondering, was that more of just calling attention to the problems, or do you feel like there were some good recommendations out of that? Do you that you need to continue that, to get all these parties together and discuss all these things to see is there a middle ground here, is there a compromise solution between those who want higher user fees and those who do not want them, or those who are opposed to higher fuel taxes? It looks like we have got to do something.

Ms. BLAKEY. Congressman Duncan, I will tell you, we have had very good feedback from that forum on the Trust Fund because it

was genuinely arranged to give the entire stakeholder community an opportunity to talk together and explore options. We had a number of panelists come in who talked about different systems, both within the U.S. Government. For example, the Food and Drug Administration, and TVA were there, as well as experts from abroad, talking about the way they have set their systems up and the pros and cons. But we also discussed options that were independent of other models.

I think what I sense coming out of that is we should certainly not rush to a solution here. It is very complex and complicated, and I think there are things we simply do not know right now that are important to analyze. But I do believe that there is a growing awareness that our costs and revenues need to be better aligned. For a system that will go into place instead of taxes and fees, whatever it may be--the last one was in place for ten years--with that prospect in front of us, it is very important at this point that we look at something that will create the right incentives both for the FAA to control its costs, as well as for the user community to take account of what the services cost.

There is a real difference between want and need. I think we do need to have, therefore, a better alignment between the cost of the service and the revenue coming in. Plus, I think there is a genuine consensus out there that it is very important that the revenues address the kind of capital investment that the next generation system will require. The answer to bringing down our costs is a system that can handle three times the traffic with a much greater degree of technology involvement, so that you bring the unit costs down which lower the costs for all of the users. Certainly, that is something that I think the airline community, in particular, would support. So how to get there, that piece we do not know yet.

Mr. DUNCAN. Well I know it is going to be very difficult to get there. But I also do not think there is anybody that has looked into this at all that has to hear much more about what the problem is. We just need to get down to the recommendations and the solutions that hopefully will be as fair as possible to the largest number. Thank you very much.

Mr. MICA. Thank you. Ms. Millender-McDonald?

Ms. MILLENDER-MCDONALD. Thank you, Mr. Chairman and Ranking Member, for such a really informative hearing. I would like to ask unanimous consent that I put my full statement in the record.

Mr. MICA. Without objection, so ordered.

Ms. MILLENDER-MCDONALD. Thank you, Mr. Chairman.

Ms. Blakey, getting back to the question that Ms. Berkley asked of you with reference to the considerable debate last year on the reauthorization, 2003. One of those towers of the 71 that FAA is contemplating it seems contracting out or privatization, I suppose, is that of my Long Beach Airport. Long Beach is the 30th busiest airport in the Nation. Again, I am not sure that I understood your answer to the question that she raised, and that was, do you have any plans on contracting out of the FAA air traffic control facilities?

Ms. BLAKEY. I would actually point out that list of 71 is not my list. This is a list that the Inspector General, who is sitting right

next to me, developed. So the specifics on the towers that are on that list and why, I would refer to him at this point.

It should tell you something that I honestly cannot even tell you about the specifics on Long Beach right now. It has been that long since I have looked at that list. So I would repeat what I said to her, which is that we have no current plans to convert those towers.

Ms. MILLENDER-MCDONALD. In other words, the 71 towers that are on the list was really initiated by the Inspector General.

Inspector General, how did you come about with that list?

Mr. MEAD. Your airport is not on the list and that list is not ours--it was a list that FAA put together in the late 1990's. We anchored our studym which was done at the request of Congress, on FAA's list.

Ms. MILLENDER-MCDONALD. It is not?

Mr. MEAD. It is not among the 71.

Ms. MILLENDER-MCDONALD. Well thank God for that.

Mr. MEAD. The list of 71 is a list of VFR towers that are currently staffed by FAA controllers and is comparable in levels of activity to those airports that are staffed by contract controllers, that are under contract with FAA to provide air traffic control services. But Long Beach is not in the 71.

Ms. MILLENDER-MCDONALD. I heard just a couple of months ago that there were some towers that were going to be closed down late at night into early morning. Is that a report that is accurate? And if so, why are we doing that when many of us are flying two and three times a week in the air and we do not wish to see any towers being closed down during a certain period? Was that a fair report?

Ms. BLAKEY. Earlier this winter, a list of I believe it was 42, if I am recalling correctly, 41 or 42 towers was put out by the news media as ones that the FAA is looking at because the fact is that, between roughly midnight and 5:00 a.m., they have very little traffic. This is a routine analysis that the FAA has done for many years on an annual basis. When traffic falls to so low at night that the Maytag repairman would look busy, it only makes sense to consider whether or not you need to have personnel from midnight to 5:00 a.m. in the tower. It does not mean that the airport does not have service. What it means is that the control of aircraft coming in passes to the nearby TRACON. So there is no reduction in service when that happens.

It is a routine analysis. It is one that is going on right now. We discussed a bit earlier today the fact that it is hard to be absolutely predictive about how long it will take, but we are doing the analysis on a case by case basis at each one of those airports to see if there are mitigating factors in terms of National Guard activity or certain other kinds of things that might call for us to continue to keep personnel on that limited shift. Otherwise, the tower is open and things remain the same. But this is an analysis, as I say, we do routinely year-in and year-out. We stopped doing it from 9/11 on because we knew traffic had dropped so much during that very unusual time that we let a few years go by before we did it again because we wanted to give all these airports a chance for the traffic to come back.

Ms. MILLENDER-MCDONALD. Thank you so much. Ms. Blakey, in your testimony you stated that over the past four years the FAA's revenue projection has been overly optimistic due to the events of September 11 and structural changes in the airline industry. Have your forecasting methodologies been appropriately adjusted to account for these issues, because there are some aviation groups that believe until FAA can accurately predict or project its cost-to-needs there cannot be reforms made to a system that may or may not be in trouble

Ms. BLAKEY. I am glad you asked that, because forecasting is something that is certainly critical and yet is extremely hard to do. As you look at any of the forecasts that are being done by Wall Street, the major corporate entities who have huge interests in this, getting that right is something that is extremely hard. And I will tell you, you are quite right that the FAA's forecasting models have been too rosy. The revenue has not come in as we had projected. In some cases it has been off as much as 11 percent a year. So we are doing an analysis right now and bringing in outside consulting help to help us develop a better forecasting model, a way of projecting those revenues.

The FAA's costs, of course, also are ones that you have to adjust on the basis of forecasted traffic. So we are trying to get that right as well as. We are doing everything we know to do to bring down our costs, such as the things we just talked about, about reducing staffing where you do not have traffic on a midnight shift, to try to do everything we can to get our costs as low as possible.

Ms. MILLENDER-MCDONALD. Thank you so very much. Mr. Inspector General, I would like to see your revised list of 71 airports. Will you please send that to my office?

Mr. MEAD. Yes. Let me clarify for the record. I misspoke. Long Beach is on the list of 71.

Ms. MILLENDER-MCDONALD. Aha.

Mr. MEAD. I misspoke. We felt, after our analysis, that the airport was not sufficiently comparable to the contract tower airports to be considered for contracting out.

Ms. MILLENDER-MCDONALD. Are you saying Long Beach is not comparable to the other airports?

Mr. MEAD. It is a very busy place, as you pointed out.

Ms. MILLENDER-MCDONALD. It is busy, yes.

Mr. MEAD. There are about 31 in the country that are quite comparable and that airport is not one of them. That is what I should have said. It is in the list of 71, but we do not feel it is sufficiently comparable.

Ms. MILLENDER-MCDONALD. And comparable is defined as what?

Mr. MEAD. Well, by level of activity. There is a lot of activity at that airport.

Ms. MILLENDER-MCDONALD. There is a lot of activity, sir. Can you provide for me your report on that and the methodology by which these airports were placed on the list?

Mr. MEAD. I will be glad to.

[The information received follows:]

MEAD

Office of Inspector General

Audit Report

Contract Towers: Observations on FAA's Study of Expanding the Program

Federal Aviation Administration

Report No. AV-2000-079
Date Issued: April 12, 2000

DEPARTMENT OF TRANSPORTATION
UNITED STATES OF AMERICA

Memorandum

U.S. Department of Transportation
Office of the Secretary
Of Transportation
Office of Inspector General

Subject: ACTION: Report on Contract Towers: Observations on FAA's Study of Expanding the Program, AV-2000-079

Date: April 12, 2000

From: Alexis M. Stefani
Assistant Inspector General for Auditing

Reply to Attn of: Dobbs:x60500

To: Federal Aviation Administrator

In response to the request in the Conference Report for the Department of Transportation and Related Agencies Appropriations Act for Fiscal Year 2000, the Office of Inspector General reviewed the Federal Aviation Administration's (FAA) Contract Tower Program (Program). This report provides the information presented to the Appropriations Committees for your information and use.

Our review answered two objectives. The first objective was to determine if previously identified concerns regarding staffing at contract towers have been corrected. The second objective was to evaluate the accuracy and completeness of FAA's study of expanding the Contract Tower Program to ensure all relevant costs and benefits were appropriately identified and considered.

We found that contract towers continue to provide services that are comparable to the quality and safety of FAA-operated towers. Users remain supportive of the Program and previously identified staffing issues have been addressed. We also found that FAA's study did not fully consider several key factors of expanding the Program that should be further analyzed and reported to Congress. We are recommending that FAA revise its draft study of expanding the Contract Tower Program to provide Congress a better perspective of the feasibility, costs and benefits of expanding the Program.

During our audit, we met with the Acting Deputy Administrator regarding our findings and recommendations and have taken his comments into consideration in preparing this report.

In accordance with Department of Transportation Order 8000.1C, we would appreciate receiving your written comments within 30 days. If you concur with our findings and recommendations, please indicate for each recommendation the specific action taken or planned and the target dates for completion. If you do not concur, please provide your rationale. Furthermore, you may provide alternative courses of action that you believe would resolve the issues presented in this report.

We appreciate the cooperation and assistance provided by you and your staff during the audit. If you have any questions or need further information, please contact me at x61992 or David Dobbs, Deputy Assistant Inspector General for Aviation, at x60500.

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EXECUTIVE SUMMARY

Contract Towers: Observations on FAA's Study of Expanding the Program

Federal Aviation Administration

Report No. AV-2000-079 *April 12, 2000*

Background

The Federal Aviation Administration (FAA) began contracting out air traffic services at low activity (Level I) towers in 1982 as a result of the Professional Air Traffic Controllers Organization strike. In 1993, Vice President Gore's National Performance Review endorsed the Contract Tower Program (Program) as an effective means of reinventing government services. Currently, there are 187 towers in the Contract Tower Program operated by 3 contractors. In July 1999, FAA issued a new solicitation for the Contract Tower Program, but as of April 2000, had not awarded final contracts.

FAA's Contract Tower Program has been successful in providing air traffic control services at low activity airports at lower costs than the agency could otherwise provide. FAA's current Contract Tower Program saves the agency about $250,000 per tower, annually. The Program also provides service at towers that FAA would otherwise not have staffed because they were too expensive to operate. In light of the Program's success, Congress last year directed FAA to conduct a study to determine if additional savings could be achieved by expanding the Contract Tower Program to other FAA-operated air traffic control towers "without radar capability." FAA currently operates 71 visual flight rules (VFR) air traffic control towers employing about 960 controllers. (Exhibit A provides a list of the 71 towers and certain statistical information about each facility.)

Prior Coverage

In 1998 we conducted a comprehensive review of the Contract Tower Program and found little difference in the quality or safety of services provided at Level I towers whether they were operated by FAA or by contractors. Specifically, we found that contract controllers met qualification requirements and received required training, users were satisfied with the services they received at contract locations, and the number and types of incidents at FAA and contract towers were comparable.

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We also found that contract towers reduced operating costs. However, we found that not all contract towers were staffed according to contract staffing plans. We recommended that FAA direct contractors to staff contract towers in accordance with contract requirements and establish procedures to periodically review staffing levels at contract towers. Those measures were necessary because contract towers were staffed with fewer controllers than FAA-operated towers and staffing levels were based on contractor-prepared staffing plans.

Objectives

This review was conducted at the request of Congress in the Department of Transportation and Related Agencies Fiscal Year (FY) 2000 Appropriations. The objectives of our review were to (1) determine if contract towers were being staffed in accordance with contract requirements and assess FAA's oversight of contractor compliance, and (2) evaluate the accuracy and completeness of FAA's study of expanding the Contract Tower Program to determine whether all relevant costs and benefits were appropriately identified and considered. (Exhibit B contains the scope of our review and the methodology used in conducting it.)

Results in Brief

Contract towers continue to provide cost-effective services that are comparable to the quality and safety of FAA-operated towers. For example, the level of operational errors in FY 1999 at contract towers was comparable to the level of operational errors at FAA VFR towers. The Contract Tower Program also provides services at towers that FAA would otherwise not have staffed because they were too expensive to operate. Users remain very supportive of the Program and believe that the services they receive at contract towers are comparable to FAA-operated towers.

We also found that previously reported staffing issues have been addressed. We tested payroll records for a 2-month period at 37 contract towers and found that contractors (in total) provided the required number of employees and hours within 2 percent of the contractual requirements. In addition, FAA's new contract solicitation contains specific provisions requiring contractors to report and certify monthly the number of controllers at each location and the hours they worked.

FAA completed a draft study of expanding the Contract Tower Program in September 1999, but as of April 2000, had not issued a final report to Congress. In the draft study, FAA concluded that no net savings would be realized from

further expanding the Program because of an agreement with the National Air Traffic Controllers Association (NATCA) that establishes a baseline staffing level of 15,000 FAA controllers through 2001. FAA agreed to increase that level by an additional 2 percent each year for the remaining 2 years of the agreement.

While the decision to expand the Contract Tower Program is ultimately a policy determination that Congress will have to weigh, FAA's study did not adequately consider several key factors of the feasibility, costs, and benefits of expanding the Program that should be further analyzed and reported to Congress.

First. FAA's methodology for determining which towers to consider did not accurately reflect the feasibility of expanding the Program. For purposes of its study, FAA narrowly defined the congressional request to evaluate FAA towers "without radar capability" and concluded that only 41 of its 71 VFR towers met the definition of Congress. FAA excluded the remaining 30 towers from consideration because those facilities are equipped with a monitoring device known as DBRITE (Digital Bright Radar Indicator Tower Equipment) and provide limited instrument flight rule services (IFR) through a letter of agreement (LOA) with a larger radar-equipped facility. DBRITE is a display monitor used by controllers at towers to identify and monitor aircraft – it is not a radar system and is not used in the radar control of air traffic.

We do not agree that those factors are reasonable causes for including or excluding towers from consideration. For example, there are currently as many as 40 towers in the existing Contract Tower Program that also are equipped with DBRITE displays and provide similar IFR services through LOAs with larger FAA facilities.

In addition, FAA's methodology went too far in considering some busier towers and not far enough in considering other towers with substantially lower levels of air traffic activity. For example, FAA included Pontiac/Oakland International Airport for consideration (even though this airport is among FAA's 50 busiest towers) because the facility is not equipped with a DBRITE and does not have an LOA to provide IFR operations. In contrast, FAA excluded Allegheny County Airport from consideration because the facility is equipped with a DBRITE and has an LOA for IFR operations even though this airport has an average air traffic count that is substantially less than many towers in the existing Program. FAA's experience in contract towers has primarily been with towers that have lower levels of air traffic activity.

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FAA needs a more comprehensive means for determining the extent that the Program could be expanded by taking into account factors such as volume of air traffic, types of users, and complexity of operations at each location. As part of its collective bargaining agreement with NATCA in 1998, FAA developed a new pay system for controllers based on reclassifying all its air traffic control (ATC) facilities. The new system establishes ATC Grades 3 through 12 based on the complexity of operations, the types of users, and the volume of air traffic at each location. FAA's 71 VFR towers were reclassified into ATC Grades 5 through 9.

In our opinion, the ATC Grades of the 71 towers could provide FAA a more comprehensive means for evaluating which facilities to consider. Additionally, should Congress choose to expand the Contract Tower Program, FAA will need to develop specific metrics for analyzing and reporting actual results of the Program's expansion (on a facility-by-facility basis) to ensure that system safety and efficiency are not impacted and that projected benefits are being fully realized.

Second. FAA's estimated cost savings were understated because the agency used FY 1998 cost figures. In FY 1999, costs to operate FAA towers increased as a result of the new pay system for FAA controllers. We estimate that annual average savings would be approximately $881,000 per tower. However, these savings would be subject to several offsetting expenses. For example, FAA would incur a one-time expense to relocate FAA controllers who elect to move from contracted facilities to other FAA facilities. According to FAA's FY 2001 budget submission to Congress, this cost was approximately $49,000 per move in FY 1999 for the Air Traffic Control division.

Third. FAA's conclusion did not consider important long-term benefits that could accrue from expanding the Program. To have credibility, FAA's study should have given much greater weight to the potential impact that controllers from contracted VFR towers could have in offsetting future increases in system demand and addressing existing staffing shortfalls. Contracting additional VFR tower operations would allow FAA to redistribute controllers from contracted locations (or their equivalent full-time positions) to FAA locations with the greatest forecast increases in air traffic activity. Experienced FAA controllers from contracted locations could also help alleviate existing staffing shortfalls which, in turn, could reduce FAA's overtime costs.

These benefits would be achievable while maintaining a workforce of 15,000 FAA controllers as specified in the agreement with NATCA. However, it is important to note that the agreement states ". . . its terms and conditions are subject to congressional approval."

EXECUTIVE SUMMARY

It is essential that FAA thoroughly analyze any and all opportunities to offset the rising costs of its operations. Expanding the Contract Tower Program provides the agency with one such opportunity. FAA should revise its study of expanding the Contract Tower Program to fully recognize the feasibility, costs, and benefits that expanding the Program offers. Revisions should include better methodology for determining which towers to consider, new savings estimates, and further evaluation of the benefits that controllers from contracted locations could provide in meeting projected growth in air traffic activity.

Principal Findings

The Current Contract Tower Program

Safety. As part of our review, we conducted tests on issues similar to those we identified in our 1998 report on the Contract Tower Program. We found that contract towers continue to be operated as safely as FAA-operated towers. For example, we found that the level of operational errors in FY 1999 at contract towers (.05 errors per 100,000 operations) was similar to the level of operational errors at comparable FAA VFR towers (.06 errors per 100,000 operations). In addition, we reviewed facility evaluation reports conducted by FAA's Evaluations Branch for a sample of 34 contract towers and found that none of the evaluations noted any significant safety issues at the contract towers.

Staffing. We also conducted a follow-up review of staffing issues noted in our 1998 report. We reviewed contractor payroll records for a sample of approximately 4 biweekly pay periods (2 months) in 1999 for 37 contract towers and compared the number of employees and hours provided by the contractors to the staffing requirements contained in their respective contracts. We found that contractors (in total) provided the required number of employees and hours within 2 percent of the contractual requirements.

In addition, we found that FAA's new contract solicitation contains specific provisions requiring contractors to report and certify monthly the number of controllers at each location and the hours they worked. These procedures should help ensure that contractors adhere to required facility-staffing plans under the new contract.

Users. Lastly, we discussed the Contract Tower Program and its proposed expansion with users at contract locations and at proposed locations. Users at contract locations continue to be supportive of the Contract Tower Program and believe the services they receive are comparable to FAA-operated towers. Based

on their experiences with the Contract Tower Program, these users felt that expanding the Program to other FAA VFR towers would be feasible. At proposed locations, most users were concerned only that the level of service they receive would remain the same if their towers were converted to contract operations.

However, other users were strictly opposed to expanding the Program. For example, one airport director told us that he used the fact that his tower was operated by the FAA as a marketing tool to attract foreign air carriers and encourage commercial service. Other groups, such as NATCA, oppose expanding the Program for other reasons. NATCA believes that expanding the Program to busier FAA VFR towers would represent a serious departure from confines of the existing Program because the number and complexity of operations at FAA's 71 VFR towers are significantly higher than operations at current contract towers.

While 15 of FAA's 71 VFR towers are busier than towers in the existing Program, the remaining 56 VFR towers have, in our opinion, operations that are comparable to towers in the existing Program. These differences underscore the complexities involved in evaluating the feasibility of expanding the Contract Tower Program. They also underscore the need for FAA to develop specific metrics for analyzing actual results of the Program's expansion to ensure that system safety and efficiency are not affected.

FAA's Study of Expanding the Contract Tower Program

FAA completed a draft study of expanding the Contract Tower Program in September 1999, but as of April 2000, had not issued a final report to Congress. In its study, FAA concluded that no savings would be realized from expanding the Program because of an agreement with NATCA that establishes a baseline staffing level of 15,000 FAA controllers. However, FAA's study did not adequately consider several key factors of the feasibility, costs, and benefits of expanding the Program that should be further analyzed and reported to Congress. These include developing better methodology for considering which towers to convert, and evaluating additional cost savings and other benefits that expanding the Program could offer.

Methodology. FAA narrowly defined the congressional request to evaluate FAA towers "without radar capability" and included only 41 of its 71 VFR towers in its study. FAA concluded that the remaining 30 towers did not meet the definition of Congress because those facilities are equipped with a monitoring device known as DBRITE and provide limited IFR services through an LOA with a larger radar-equipped facility. We do not agree that those factors are reasonable causes for

including or excluding towers from consideration. For example, there are currently as many as 40 towers in the existing Contract Tower Program that also are equipped with DBRITE displays and provide similar IFR services through LOAs with larger FAA facilities.

In addition, FAA's methodology went too far in considering some busier towers and not far enough in considering other towers with substantially lower levels of air traffic activity. For example, FAA included Pontiac/Oakland International Airport for consideration (even though this airport is among FAA's 50 busiest towers) because the facility is not equipped with a DBRITE and does not have an LOA for IFR operations. In contrast, FAA excluded Allegheny County Airport from consideration because the facility is equipped with a DBRITE and has an LOA for IFR operations even though this airport has an average air traffic count of only about 28 aircraft per hour (less than many towers in the existing Program).

In 1998, FAA reclassified all its air traffic control facilities into ATC Grades 3 through 12 based on numerous factors including the complexity of operations, types of users, and the volume of air traffic handled at each location. For example, under FAA's old grade structure, Chicago O'Hare and JFK International were both classified as Level V facilities but in 1998 were reclassified as ATC Grades 12 and 10, respectively.

Although FAA's 71 VFR towers were reclassified into ATC Grades 5 through 9, FAA did not use ATC Grades to determine which facilities to include in its study. As a result, FAA did not consider important differences about the 71 VFR towers such as the volume of air traffic they control, the types of users they serve, and complexity of operations they manage. For example, the average hourly traffic density at the 71 towers ranges from 28 aircraft per hour to over 118 aircraft per hour – 11 of the 71 towers are among FAA's 50 busiest towers. One tower, Van Nuys, California, (an ATC Grade 9) is the fifth busiest air traffic control tower in the country – busier than towers such as Miami International, Detroit Metropolitan, and Boston Logan.

In our opinion, the ATC Grades of the 71 towers offer Congress and FAA a more comprehensive means for evaluating which facilities to consider by taking into account factors such as the volume of air traffic, the types of users, and the complexity of operations at each location. Additionally, should Congress choose to expand the Contract Tower Program, FAA will need to develop specific metrics for analyzing and reporting actual results of the Program's expansion (on a facility-by-facility basis) to ensure that system safety and efficiency are not affected and that projected benefits are being fully realized.

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Estimated Savings. FAA estimated that the agency would realize average annual savings of about $787,000 per facility by expanding the Program. FAA's estimate was based on a framework using Office of Management and Budget Circular A-76 requirements for cost comparisons. We tested the costs used in FAA's estimate and found that the underlying data were reasonable. However, FAA's estimates were developed using FY 1998 costs. In FY 1999, the costs of operating FAA towers increased as a result of the new pay system for FAA controllers.

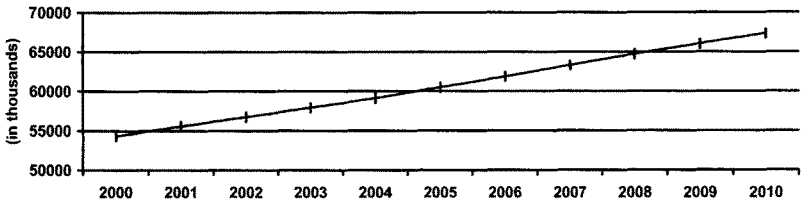
Using FAA's methodology and actual contract and agency costs for FY 1999, we estimate that annual average savings could be approximately $881,000 per tower. (Exhibit C provides details of these estimates.) These savings would be subject to several offsetting expenses, however. For example, FAA would incur a one-time expense to relocate FAA controllers who elect to move from contracted facilities to other FAA facilities. According to FAA's FY 2001 budget submission to Congress, this cost was approximately $49,000 per move in FY 1999 for the Air Traffic Control division.

FAA's Conclusions. In its study, FAA concluded that no savings could be realized from expanding the Contract Tower Program because of a July 1998 Memorandum of Agreement between FAA and NATCA. Article I of that agreement establishes a baseline staffing level of 15,000 controllers for FYs 1999 through 2001, increasing by an additional 2 percent each year for the remaining 2 years of the agreement. FAA agreed to maintain those numbers when attrition, transfers, or promotions reduced those levels. As a result of those requirements, FAA concluded there could be no net savings from expanding the Program because the agreement prohibits a decrease in the number of FAA personnel.

FAA's conclusion is based on a premise that there could be no savings from expanding the Contract Tower Program because the agency would have to increase the costs of the Program while maintaining the same level of FAA controllers. However, FAA's conclusion ignores other long-term benefits that would accrue from expanding the Program. For example, controllers from contracted towers could have a significant impact in meeting projected increases in air traffic demand. As shown in the following graph, FAA is forecasting aircraft operations at airports with FAA-operated air traffic services to increase from about 54 million in 2000 to over 67 million in 2010 – an increase of over 24 percent.

EXECUTIVE SUMMARY

Forecast Aircraft Operations at Airports with FAA-Operated Air Traffic Services



FAA's study should have given greater merit to the potential impact that controllers from contracted VFR towers could have in offsetting potential future increases in system demands. Contracting out additional VFR tower operations would allow the agency to redistribute controllers (or their equivalent full-time positions) from contract locations to FAA locations with the greatest forecast increases.

Experienced controllers from the 71 facilities would also reduce FAA's projected hiring needs thus reducing costs associated with training newly hired controllers. FAA spends approximately $47,000 per employee to provide newly hired controllers initial air traffic control training. According to FAA officials, the agency is projecting to hire approximately 2,000 new controllers over the next 4 years.

In addition, experienced FAA controllers from contracted locations could help alleviate existing staffing deficiencies. For example, as of December 1999, the Los Angeles International Airport tower was understaffed by eight controllers. If the Program were expanded, the 13 controllers assigned to the Santa Monica tower (or their equivalent full-time positions) could be reassigned to Los Angeles International to address that facility's staffing needs. Actions such as these would also help FAA reduce overtime expenditures at understaffed facilities. In FY 1999, FAA incurred over $19 million in overtime costs to meet operational needs at its air traffic control facilities.

FAA should more carefully examine the potential benefits that expanding the Contract Tower Program could provide in addressing staffing deficiencies and ensuring that FAA has sufficient resources at key locations to meet projected increases in air traffic activity.

EXECUTIVE SUMMARY

Recommendations

We recommend that FAA revise its draft study of expanding the Contract Tower Program to provide Congress a better perspective of the feasibility, costs, and benefits of expanding the Program. Revisions to the study should, at a minimum, include:

- a new listing of towers that could be contracted using FAA ATC Grades as the methodology for determining which towers to consider;
- new cost savings estimates using FY 1999 actual contract and agency costs; and
- evaluation of the potential benefits that controllers from contracted towers could provide in addressing staffing imbalances and ensuring that the agency has sufficient resources at key locations to meet projected increases in demand.

Additionally, should Congress choose to expand the Contract Tower Program, we recommend that FAA develop specific metrics for analyzing and reporting actual results of the Program's expansion (on a facility-by-facility basis) to ensure that system safety and efficiency are not impacted and that projected benefits are being fully realized.

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The Current Contract Tower Program

The Federal Aviation Administration's (FAA) Contract Tower Program (Program) has proven successful in providing air traffic control services at low activity airports at lower costs than the agency could otherwise provide. The Program also provides service at towers that FAA would otherwise not have staffed because they were too expensive to operate. According to FAA, significant cost savings have been achieved, air traffic services have been maintained without derogating safety, and the quality of service to the customer has been maintained at a high level. In its study of expanding the Contract Tower Program, FAA states:

> Services provided at a [contract tower] are identical to those provided at an FAA-staffed [tower]. Contract air traffic controllers are certified by FAA and must follow appropriate Code of Federal Regulations and FAA directives. The change to contractor-provided air traffic control services is transparent to users.

In 1998, we conducted a comprehensive review of the Contract Tower Program and came to many of the same conclusions as FAA. We found little difference in the quality or safety of services provided at Level I towers whether they were operated by FAA or by contractors. Specifically, we found that (1) contract controllers met qualification requirements; (2) contract controllers received required training; (3) users were satisfied with contract tower services; and (4) the number and types of incidents at FAA and contract towers were comparable.

We also found that the Contract Tower Program reduced FAA's operations costs. The current Contract Tower Program saves the agency about $250,000 per tower, annually. However, we found that some contract towers were not staffed in accordance with contract terms.

We recommended that FAA closely monitor contract tower staffing levels. This was necessary because (1) contract towers are staffed with fewer controllers than FAA-operated towers, and (2) staffing levels were based on contractor-prepared staffing plans. FAA agreed to those plans because the agency does not have precise standards for estimating staffing requirements for individual facilities.

As part of our current review, we conducted tests similar to those we did in 1998. Specifically, we wanted to determine (1) if the Program continues to operate safely, (2) if previously identified staffing issues have been addressed, and (3) if users continue to be satisfied with the Program.

Safety. Contract towers continue to be operated as safely as FAA-operated towers. For example, we found that the level of operational errors and deviations in Fiscal Year (FY) 1999 at contract towers (.05 per 100,000 operations) was similar to the level of incidents at a sample of comparable FAA visual flight rules (VFR) towers[1] (.06 per 100,000 operations).

In addition, we reviewed a sample of facility evaluation reports conducted by FAA's Evaluations Branch for contract towers. The Evaluations Branch conducts extensive biennial full-facility reviews of all air traffic facilities. Our sample included the most recent evaluations conducted at 34 contract towers. None of the evaluations we reviewed noted any significant safety issues at the contract towers.

Staffing. We also conducted a follow-up review of staffing issues noted in our 1998 audit. We reviewed contractor payroll records for a sample of approximately 4 biweekly pay periods (2 months) in 1999 for 37 contract towers. We then compared the number of employees and hours provided by the contractors to the staffing requirements contained in their respective contracts. As shown in the following table, we found that contractors (in total) provided the required number of employees and hours within 2 percent of the contractual requirements.

STAFFING SAMPLE RESULTS BY CONTRACTOR

	Controllers*			Hours per Pay Period			
Company	Pay Records	Contract Terms	Difference	Pay Records	Contract Terms	Difference	%
1	268	268	0	19,868	20,220	(352)	(2)%
2	196	190	6	13,737	13,664	73	1%
3	300	300	0	21,304	21,492	(188)	(1)%

*These figures represent the total number of controller pay records for 4 biweekly pay periods in our sample. They do not reflect the actual number of controllers employed at the towers reviewed.

FAA has also specifically addressed facility-staffing variances in its new contract solicitation. The new contract contains three provisions addressing staffing issues that should strengthen the agency's oversight of the Contract Tower Program. First, the new contract requires the contractor to submit a monthly report to the FAA Contract Tower Program Office including such items as total hours worked and the number of facility-rated controllers working each month.

Second, the new contract addresses overstaffing and understaffing at facilities. If a contract tower is overstaffed by more than 3 percent above the agreed upon staffing plan, without prior approval from the FAA contracting officer, the agency

[1] Our sample included only FAA towers in ATC Grades 5 and 6, which are most similar to the operations at towers in the existing Contract Tower Program.

could deny payment to the contractor for the hours worked that exceeded the staffing plan. Similarly, FAA could recoup any payments made to the contractor if a facility were understaffed by 3 or more percent. Third, under the new contract, the contractor must certify that the hours billed under the contract are the actual hours worked during each quarter.

These reports should enable the Contract Tower Program Office to track hours of service provided by the contractor and verify that the contractually specified staffing standards are met. FAA will also be able to adjust payments made to the contractor based on the hours of service provided and billed to FAA. For these procedures to be effective, however, FAA will need to periodically audit the reported data on a more frequent basis and ensure that penalties for noncompliance are clear and strictly enforced.

User Perspectives. We discussed the Contract Tower Program and its proposed expansion with users at contract locations, at proposed locations, and with outside organizations. We found that users at contract locations continue to be supportive of the Contract Tower Program. In general, these users told us that the services they receive from contractors are comparable to FAA-operated towers and that they were satisfied with the overall quality and safety of contract operations. Based on their experiences with the Contract Tower Program, these users felt that expanding the Program to other FAA VFR towers would be feasible. At proposed locations, most users were concerned only that the level of service they receive would remain the same if their towers were converted to contract operations.

However, other users were strictly opposed to expanding the Program. For example, one airport director told us that he used the fact that his tower was operated by the FAA as a marketing tool to attract foreign air carriers and encourage commercial service. Other groups, such as the National Air Traffic Controllers Association (NATCA), oppose expanding the Program. NATCA believes that expanding the Program to busier FAA VFR towers would represent a serious departure from the existing Program because the number and complexity of operations at FAA's 71 VFR towers are significantly higher than operations at current contract towers.

While 15 of FAA's 71 VFR towers are busier than towers in the existing Program, the remaining 56 VFR towers have, in our opinion, operations that are comparable to towers in the existing Program. These differences underscore the complexities involved in evaluating the feasibility of expanding the Contract Tower Program. They also underscore the need for FAA to develop specific metrics for analyzing actual results of the Program's expansion to ensure that system safety and efficiency are not affected.

FAA's Study of Expanding the Contract Tower Program

FAA completed a draft study of expanding the Contract Tower Program in September 1999, but as of April 2000 had not issued a final report to Congress. In the draft study FAA concluded that no net savings would be realized from further expanding the Program because of an agreement with NATCA that establishes a baseline staffing level of 15,000 FAA controllers.

While the decision to expand the Contract Tower Program is ultimately a policy determination that Congress will have to weigh, FAA's study did not adequately consider several key factors of the feasibility, costs, and benefits of expanding the Program that should be further analyzed and reported to Congress. These include developing better methodology for considering which towers to convert, and evaluating additional cost savings and other benefits that could be realized from expanding the Program.

I. Better Methodology Is Needed for Considering Which Towers to Convert

FAA narrowly defined the congressional request to evaluate FAA towers "without radar capability." For purposes of its study, FAA defined 41 of the 71 VFR towers as meeting the congressional definition. FAA excluded the remaining 30 towers from the study because those facilities were equipped with a monitoring device known as DBRITE[2] and provided limited instrument flight rule (IFR) services through a letter of agreement (LOA) with a larger radar-equipped facility.

We do not agree that those factors are reasonable causes for including or excluding towers from consideration. For example, there are currently as many as 40 towers in the existing Contract Tower Program that also are equipped with DBRITE displays and provide similar IFR services through LOAs with larger FAA facilities.

We observed operations at 15 of the contract towers with LOAs and compared their operations to 12 of the 30 FAA towers excluded from the study. We concluded that, other than the level of air traffic activity, there were no differences in the nature or types of operations conducted at those facilities.

The methodology FAA used would also result in some lower activity towers being excluded from consideration while busier and larger facilities would be considered for conversion to contract operations. For example, using FAA's methodology,

[2] DBRITE (Digital Bright Radar Indicator Tower Equipment) is a display monitor used by controllers at towers to identify aircraft and monitor their position. DBRITE is not a radar system and is not used in radar control of air traffic.

Ann Arbor Municipal Airport (with an average air traffic count of **43 aircraft per hour**) would be excluded from consideration because the facility is equipped with a DBRITE and has an LOA for IFR operations with a larger FAA facility. In contrast, Pontiac/Oakland International Airport (with an average air traffic count of **76 aircraft per hour**) would be considered for conversion because the facility is not equipped with DBRITE and does not have an LOA for IFR operations with another FAA facility.

Significant Differences Among FAA's 71 VFR Towers Need to Be Considered. The methodology used by FAA did not adequately consider important differences about the 71 VFR towers. Unlike most towers in the Contract Tower Program which are relatively similar (primarily low activity general aviation airports), FAA's 71 VFR towers are not a homogeneous group. These facilities have significant differences in the volume of air traffic they control, the number and types of users they serve, and the complexity of the airspace they manage. For example, the average hourly traffic density at the 71 VFR towers ranges from 28 aircraft per hour to over 118 aircraft per hour. One VFR tower, Van Nuys, California, is the fifth busiest air traffic control tower in the country. In all, 11 of the 71 VFR towers are among FAA's top 50 busiest air traffic control towers in the United States.

The mix and types of users at the 71 locations also vary extensively. For example, many of these towers handle only general aviation aircraft while others have daily commercial jet service. For example, Long Beach, California, has daily domestic service from American and America West Airlines, and Orlando Sanford, Florida, has regularly scheduled international service from Europe.

Finally, the complexity of the airspace controlled varies among the 71 VFR towers. Several towers have relatively simple and open airspace while others must interact extensively with larger and busier airports. For example, Orlando Executive's airspace lies directly under a major approach and departure path for Orlando International Airport. These factors, at a minimum, should be included in any criteria used to determine which facilities should or should not be considered for conversion to contract operations.

FAA ATC Grades Could Provide a Better Means for Evaluating Towers. Although many of the differences between FAA's 71 VFR towers have already been taken into account under FAA's reclassification efforts, FAA did not use ATC Grades in determining which towers to consider. In 1998, FAA reclassified all its air traffic control facilities into ATC Grades 3 through 12 based on various factors including the volume of air traffic and complexity of operations at each location.

Under the new system, facilities that were previously rated at the same level may have been reclassified into different ATC Grades. For example, under FAA's old classification system, air traffic control towers at the Chicago O'Hare and John F. Kennedy airports were classified as Level V facilities, but under the new system the facilities were reclassified as ATC Grades 12 and 10, respectively. As shown in the following table, the 71 VFR towers have been reclassified into ATC Grades 5 through 9.

ATC GRADES OF FAA's 71 VFR TOWERS

ATC GRADE	TOWERS	CONTROLLERS*
5	10	110
6	25	301
7	28	372
8	4	75
9	4	101
Total	**71**	**959**

*As of December 1999.

In our opinion, the ATC Grades of the 71 towers offer Congress and FAA a more comprehensive means for evaluating which facilities to consider by taking into account factors such as the volume of air traffic, the types of users, and the complexity of operations at each location. Additionally, should Congress choose to expand the Contract Tower Program, FAA will need to develop specific metrics for analyzing and reporting actual results of the Program's expansion (on a facility-by-facility basis) to ensure that system safety and efficiency are not affected and that projected benefits are being fully realized.

II. Additional Cost Savings Could be Realized by Expanding the Program

FAA estimates that contracting out its VFR towers could result in average annual savings of approximately $787,000 per facility. FAA's cost comparison was conducted by averaging the annual costs of 12 facilities with high air traffic density already in the Contract Tower Program with 12 of the 71 FAA facilities with similar density counts. FAA's methodology was based on a framework using Office of Management and Budget Circular A-76 requirements for cost comparisons. We tested the costs used in FAA's estimate and found that the underlying data were reasonable.

The estimated savings from expanding the Contract Tower Program could be greater, however. FAA's estimates were based on using FY 1998 costs. In FY 1999, FAA salary costs increased as a result of a new pay system for FAA controllers, which in turn increased the costs of operating FAA towers.

OIG Estimated Savings. Using FAA's methodology and actual contract and agency costs for FY 1999, we recalculated the potential savings of expanding the Contract Tower Program. We estimate that annual average savings could be as much as $881,000 per tower, or approximately $62.5 million if all 71 VFR towers were contracted out.

The cost of operating FAA's 71 towers will increase further as a result of new pay differential for FAA controllers. In November 1999, FAA and NATCA agreed to implement a Controller Incentive Pay for controllers at high-cost-of-living locations. FAA controllers at 30 of the 71 locations began receiving an additional pay differential between 5 and 10 percent in FY 2000.

Contract Costs May Be Higher Than Estimated. Actual contract costs may be higher than the average used in FAA's estimate for several reasons.

- First, contractors would have to staff some of the 71 FAA facilities with more controllers than they use at existing contract towers because of the higher levels of air traffic activity.

- Second, contractors would most likely have to develop a tiered pay system (like FAA's pay system for controllers) to attract and retain qualified contract controllers at facilities that are busier and more complex than towers in the existing Program.

- Third, because of the complexity of some of the FAA facilities, contract controllers would require more time to become facility certified than controllers in the current Program require. FAA and contract officials estimated it would require controllers between 60 and 90 days to qualify. During this period, FAA incurs costs of the contract as well as the salary costs for FAA employees.

- Lastly, FAA would incur a one-time cost to relocate FAA controllers from contracted out facilities to other FAA facilities. According to FAA's FY 2001 budget submission to Congress, this cost was approximately $49,000 per move in FY 1999 for the Air Traffic Control division. It is important to note, however, that not all controllers would relocate. Some controllers would retire, some would choose to work for the contractors, and others could be reassigned to nearby FAA facilities that would not require them to relocate.

FAA's Contract Tower Program Office is aware of each of these issues and is making plans to address them should the Contract Tower Program be expanded.

III. Other Benefits Should Be Considered

FAA concluded that there would be no savings realized from expanding the Contract Tower Program because of a July 1998 Memorandum of Agreement between FAA and NATCA. Article I of that agreement establishes a baseline staffing level of 15,000 controllers for FYs 1999 through 2001, increasing by 2 percent in FYs 2002 and 2003. The agreement states:

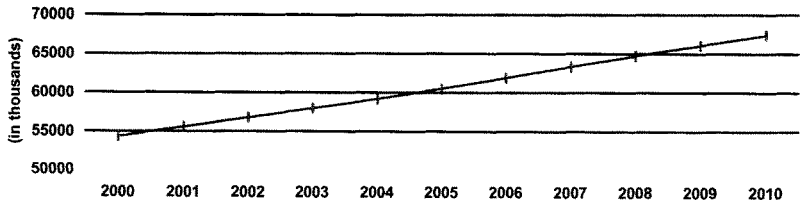
> The agency will backfill in order to maintain these numbers when attrition, transfers, or promotions reduce the staffing below the agreed upon numbers.

As a result, FAA concluded that there could be no net savings from expanding the Contract Tower Program because the agreement prohibits a decrease in the number of FAA personnel. However, this conclusion is based on only one possible outcome of expanding the Program. FAA should have more adequately considered several other options before arriving at that conclusion.

Other Considerations. While the agreement with NATCA may represent an expression of policy between the agency and union and reflect their objectives, Congress is not bound by its terms. In providing funding to and authorizing the programs and activities of FAA, Congress may exercise its constitutional prerogative by modifying the provisions or the underlying assumptions of the agreement.

Other Benefits. More importantly, other long-term benefits would accrue from expanding the Program regardless of the agreement with NATCA. Controllers from contracted towers could have a significant impact in meeting projected increases in air traffic demand. As shown in the following graph, FAA is forecasting aircraft operations at airports with FAA-operated air traffic services to increase from about 54 million operations in 2000 to over 67 million operations in 2010 – an increase of over 24 percent.

Forecast Aircraft Operations at Airports with FAA-Operated Air Traffic Services



FAA's study should have given greater merit to the potential impact that controllers from contracted VFR towers could have in offsetting potential future increases in system demands. Contracting out additional VFR tower operations would allow the agency to redistribute controllers (or their equivalent full-time positions) from contract locations to FAA locations with the greatest forecast increases.

Reassigning controllers from the 71 facilities would also reduce FAA's projected hiring needs thus reducing costs associated with training newly hired controllers. FAA spends approximately $47,000 per employee to provide newly hired controllers initial air traffic control training. According to FAA officials, the agency is planning to hire over 2,000 new controllers over the next 4 years.

Experienced FAA controllers from contracted locations could also help alleviate existing staffing deficiencies. For example, as of December 1999, the Los Angeles International Airport tower was understaffed by eight controllers. If the Program were expanded, the 13 controllers assigned to the Santa Monica tower (or their equivalent full-time positions) could be reassigned to Los Angeles International and address that facility's staffing needs. Actions such as these would also help FAA reduce overtime expenditures at understaffed facilities. In FY 1999, FAA incurred over $19 million in overtime costs to meet operational needs.

FAA should more carefully examine the potential benefits that expanding the Contract Tower Program could provide in addressing existing staffing deficiencies and ensuring that FAA has sufficient resources at key locations to meet projected increases in demand.

Recommendations

We recommend that FAA:

1. Revise its draft study of expanding the Contract Tower Program to provide Congress a better perspective of the feasibility, costs, and benefits of expanding the Program. Revisions to the study should, at a minimum, include:

    - a new listing of towers that could be contracted using FAA ATC Grades as methodology for determining which towers to consider;

    - new cost savings estimates using FY 1999 actual contract and agency costs; and

    - an evaluation of the potential benefits that controllers from contracted towers could provide in addressing staffing deficiencies and ensuring that the agency has sufficient resources at key locations to meet projected increases in air traffic activity.

2. Develop specific metrics for analyzing and reporting actual results of expanding the Program (on a facility-by-facility basis) to ensure that system safety and efficiency are not impacted should Congress choose to expand the Program.

Exhibit A
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71 VFR Towers Considered in FAA's Report to Congress on the Contract Tower Program

ATC Grade 5 VFR Towers

State	Airport	Density As of 11/99, unless noted	Staffing As of 12/31/99	Excluded in FAA's Study	Controller Incentive Pay
AK	Juneau International	39.98	10	No	0.0%
AZ	Grand Canyon Municipal	56.59	10	No	0.0%
CA	El Monte	36.23	10	No	8.0%
CA	Napa County	42.19	11	No	5.5%
CA	Santa Rosa Sonoma	35.88	12	No	5.5%
FL	Fort Pierce	38.14	13	No	0.0%
IN	Lafayette/Perdue University	45.29	11	No	0.0%
MI	Ann Arbor Municipal	43.10	12	Yes	5.0%
MI	Traverse City	35.55 (10/99)	9	No	0.0%
VA	Manassas Regional/Davis Field	27.89	12	No	5.5%
		ATC-5 Staffing	**110**		

ATC Grade 6 VFR Towers

AZ	Scottsdale	48.55	14	No	0.0%
CA	Camarillo	45.33	11	No	8.0%
CA	Concord/Buchanan Field	52.50	9	No	8.0%
CA	Hayward Air Terminal	45.65	11	No	8.0%
CA	Livermore Municipal	60.30	10	No	8.0%
CA	Sacramento International	31.70	15	Yes	0.0%
CA	San Jose/Reid-Hillview	48.56	9	No	8.0%
CO	Denver/Jeffco	38.32	15	No	0.0%
DE	Wilmington/New Castle	33.06	12	No	0.0%
FL	Miami/Kendall-Tamiami	47.30	13	Yes	0.0%
FL	Vero Beach	50.98	14	No	0.0%
IL	Cahokia/St. Louis	49.22	12	Yes	0.0%
IL	Chicago/Aurora Municipal	33.74	13	No	5.5%
KY	Louisville Bowman	38.29	11	Yes	0.0%
LA	New Orleans/Lakefront	40.91	11	Yes	0.0%
MI	Detroit Willow Run	37.28 (10/ 99)	12	Yes	4.5%
MN	Minneapolis/Crystal	48.51	11	Yes	0.0%
MN	St. Paul Downtown	39.61	12	No	0.0%
MO	Spirit of St. Louis	47.19	14	Yes	0.0%
NY	Poughkeepsie/Dutchess	33.43	8	No	0.0%
OR	Portland-Hillsboro	55.94	10	No	0.0%
PA	Northeast Philadelphia	48.86	12	No	5.5%
PA	Pittsburgh/Allegheny County	28.33	14	Yes	0.0%
TX	Fort Worth/Alliance	49.78	17	Yes	0.0%
WA	Everett Paine Field	57.75	11	No	0.0%
		ATC-6 Staffing	**301**		

ATC Grade 7 VFR Towers

State	Airport	Density As of 11/99, unless noted	Staffing As of 12/31/99	Excluded in FAA's Study	Controller Incentive Pay
AK	Anchorage/Merril Field	49.36	12	No	0.0%
AZ	Mesa/Falcon Field	56.67	13	No	0.0%
AZ	Phoenix-Deer Valley Municipal	63.74	15	No	0.0%
AZ	Prescott/EA Love Field	89.72	18	No	0.0%
CA	Carlsbad/McClellan	62.55	14	No	5.5%
CA	Chino	44.56	10	No	4.5%
CA	La Verne/Bracket Field	59.97	11	No	8.0%
CA	Palo Alto	47.99	10	No	8.0%
CA	San Diego/Gillespie Field	49.46	12	No	5.5%
CA	San Diego/Montgomery	58.04	16	No	5.5%
CA	Santa Monica Municipal	53.44	13	Yes	8.0%
CA	Torrance/Zamperini Field	51.55	10	No	8.0%
FL	Fort Lauderdale Executive	48.66 (9/99)	15	Yes	0.0%
FL	Orlando Executive	45.17	11	Yes	0.0%
GA	Atlanta/Dekalb-Peachtree	50.52	16	Yes	0.0%
IL	Chicago/Du Page	46.57 (10/99)	16	Yes	5.5%
IL	Chicago/Palwaukee Municipal	38.36	14	Yes	5.5%
MA	Bedford/Hanscom Field	46.45	13	Yes	8.0%
MA	Nantucket Memorial	39.75	9	Yes	8.0%
MN	Minneapolis/Flying Cloud	50.42	14	No	0.0%
ND	Grand Forks International	57.26	16	Yes	0.0%
NJ	Caldwell/Essex County	56.52	13	No	5.5%
NJ	Morristown Municipal	56.99	11	No	5.5%
NV	North Las Vegas	51.55	17	Yes	0.0%
NY	Farmingdale/Republic	57.75	12	No	8.0%
TX	Dallas Addison	36.48	15	Yes	0.0%
TX	Tomaball D. W. Hooks	62.02	13	Yes	0.0%
VA	Newport News	48.28	13	No	0.0%
		ATC-7 Staffing	**372**		

ATC Grade 8 VFR Towers

FL	Orlando/Sanford	78.11	18	Yes	0.0%
MI	Pontiac/Oakland Ct'y Internat'l	76.22 (6/99)	17	No	5.5%
OK	Tulsa/Riverside	70.77	17	Yes	0.0%
WA	Seattle/Boeing Field	72.68	23	Yes	5.5%
		ATC-8 Staffing	**75**		

ATC Grade 9 VFR Towers

CA	Long Beach/Daughtery	97.80	29	Yes	8.0%
CA	Van Nuys	118.35	23	Yes	8.0%
CO	Denver/Centennial	97.45	24	Yes	0.0%
TX	Fort Worth Meacham	75.97	25	Yes	0.0%
		ATC-9 Staffing	**101**		
		Total Staffing	***959***		

Scope and Methodology

This review was conducted between October 1999 and February 2000. Exhibit D lists the activities we visited or contacted during the audit. We conducted the audit in accordance with Government Auditing Standards prescribed by the Comptroller General of the United States and included such tests as we considered necessary to provide reasonable assurance of detecting abuse or illegal acts. Our methodology was designed around answering the following four questions.

Were previously identified staffing problems in the Federal Contract Tower Program corrected? To address this question, we conducted a follow-up review of staffing issues noted in our 1998 audit. We selected a judgmental sample of 37 towers and reviewed a sample of controller payroll records for approximately 4 biweekly pay periods (2 months) in 1999. We then compared the number of controllers and hours provided to staffing requirements. We also reviewed the new contract solicitation to assess FAA's procedures for oversight of contractor compliance. In addition, we reviewed a sample of the most recent facility evaluation reports conducted by FAA's Evaluations Branch.

Is FAA's claim that towers with a DBRITE and an LOA for IFR operations cannot be contracted a valid assertion? To address this question, we selected and visited a total of 27 towers (12 of the 71 FAA VFR towers and 15 contract towers). At these towers, two members of our staff (former air traffic controllers) observed air traffic operations to determine if there was a discernible difference in operations justifying excluding certain FAA towers from contract consideration. In addition, we interviewed airport management officials and users to determine if services received at contract towers are comparable to FAA-operated towers.

Were all costs and estimates used in FAA's study reasonable? To address this question, we reviewed the methodology FAA used for estimating the average annual savings. We compared FAA's methodology to Office of Management and Budget Circular A-76 requirements for cost comparisons. We also traced to source documents a sample of the costs used by FAA to determine if the underlying data were accurate. Using FY 1999 cost data and FAA's methodology, we calculated the potential average cost savings for the contract towers and FAA-operated towers.

What other costs and benefits should have been considered in FAA's study? To address this question, we reviewed FAA's FYs 1999 and 2000 budget requests to identify other cost factors that would be impacted by expanding the Contract Tower Program. These include projected increases in air traffic activity, overtime costs, training costs for new controllers, and average relocation costs. We also interviewed FAA officials responsible for training, staffing, and hiring.

Comparison of Potential Cost Savings for FY 1998 and FY 1999

FY 1998 Cost Comparison

FAA Facility	FY 98 Cost	FCT Facility	FY98 Cost
Concord, CA	$1,353,338	Anoka, MN	$423,456
Everett, WA	$1,047,324	Carbondale, IL	$299,784
Fort Pierce, FL	$1,113,654	Chandler, AZ	$392,550
Hillsboro, OR	$1,098,362	Gateway, AZ	$368,696
Juneau, AK	$1,066,483	Gwinnett, GA	$297,108
Lafayette, IN	$1,212,747	Hollywood, FL	$307,872
Livermore, CA	$1,236,710	Lakeland, FL	$382,908
Manassas, VA	$917,365	Norman, OK	$273,509
Napa, CA	$1,037,942	Pompano Beach, FL	$267,420
Santa Rosa, CA	$1,097,095	Ryan Field, AZ	$350,016
Traverse City, MI	$931,663	San Carlos, CA	$345,228
Vero Beach, FL	$1,335,207	Stewart, NY	$301,692
	$13,447,890		$4,010,239

Average FAA VFR Tower = $1,120,658
Average Contract Tower = $334,187
Average Savings = $786,471
Total Cost Savings for 71 Towers = $55,839,441

FY 1999 Cost Comparison

FAA Facility	FY99 Cost	FCT Facility	FY99 Cost
Concord, CA	$1,320,939	Anoka, MN	$427,152
Everett, WA	$1,023,432	Carbondale, IL	$305,064
Fort Pierce, FL	$1,255,938	Chandler, AZ	$431,460
Hillsboro, OR	$1,225,717	Gateway, AZ	$380,064
Juneau, AK	$1,008,362	Gwinnett, GA	$316,008
Lafayette, IN	$1,130,407	Hollywood, FL	$314,376
Livermore, CA	$1,458,186	Lakeland, FL	$384,000
Manassas, VA	$1,211,751	Norman, OK	$273,509
Napa, CA	$1,221,485	Pompano Beach, FL	$284,364
Santa Rosa, CA	$1,251,043	Ryan Field, AZ	$377,916
Traverse City, MI	$1,055,801	San Carlos, CA	$345,228
Vero Beach, FL	$1,671,332	Stewart, NY	$424,860
	$14,834,393		$4,264,001

Average FAA VFR Tower = $1,236,199
Average Contract Tower = $355,333
Average Savings = $880,866
Total Cost Savings for 71 Towers = $62,541,486

The cost comparison was conducted by averaging the annual cost of 12 high-density facilities already in the Contract Tower Program (FCT Facilities) and averaging the annual cost of 12 FAA towers with similar densities that qualified to be contracted out under FAA's draft report to Congress for both FY 1998 and FY 1999.

Activities Visited or Contacted

FAA Air Traffic Control Towers

Facility	State
Long Beach	CA
Santa Monica	CA
Torrance	CA
Van Nuys	CA
Fort Lauderdale Executive	FL
Orlando Executive	FL
Orlando Sanford	FL
Tamiami	FL
Dallas/Addison	TX
Fort Worth/Alliance	TX
Fort Worth/Meacham	TX
Seattle Boeing	WA

Federal Contract Towers (FCT)

Facility	State	Contractor
Topeka/Forbes Field	KS	Midwest
Johnson County Executive	KS	Midwest
Melbourne	FL	RVA
Naples Municipal	FL	RVA
Opa Locka	FL	RVA
Page Field	FL	RVA
Brownsville	TX	RVA
Dallas/Redbird	TX	RVA
Harlingen	TX	RVA
McAllen	TX	RVA
Fullerton	CA	Serco
Palmdale	CA	Serco
San Diego/Brown Field	CA	Serco
Renton	WA	Serco
Seattle/Tacoma Narrows	WA	Serco

FCT Contractors

Midwest Air Traffic Control Services, Olathe, KS
Robinson-VanVuren Associates, Oklahoma City, OK
Serco Management Services, Palmdale, CA

Activities Visited or Contacted (Continued)

Aviation Associations

Executive Vice President, American Association of Airport Executives, Alexandria, VA
Representatives of National Air Traffic Controllers Association

Users

California

Commander, United States Air Force, Palmdale
Airport Manager, San Diego, Brownfield
Airport Manager, Assistant Airport Manager, and Superintendent, Van Nuys Airport
Airport Noise Operations Technician, City of Santa Monica Airport Authority
Airport Operations Analyst, Long Beach
Representative, Boeing Corporation, Long Beach

Florida

Manager, General Aviation, Page Field General Aviation Airport
Manager, Government Affairs, Southwest Florida International Airport
Department Director, General Aviation/Facilities, Southwest Florida International Airport
Airport Manager, Tamiami Airport
Chief of Safety, Miami Dade County
Executive Director, City of Naples Airport Authority
Assistant Airport Manager, Fort Lauderdale Executive Airport
Representatives of World Jet, Incorporated, Fort Lauderdale
Representatives of Aero Design, Fort Lauderdale
Manager, Opa Locka Airport
Executive Director, Orlando Sanford Airport Authority
Director of Operations and Maintenance, Orlando Sanford Airport Authority
Director of General Aviation, Melbourne International Airport
Airport Operations Manager, Melbourne International Airport
Chief of Police, Melbourne Airport Police Department
Chief Flight Engineer, Surveillance & Battle Management Systems, Northrop Grumman, Melbourne
Director of Operations, Florida Institute of Technology, Melbourne
Representatives of Atlantic Jet Center, Melbourne

Kansas

President, Metro Topeka Airport Authority

Activities Visited or Contacted (Continued)

Washington
Airport Manager, Comarco Airport Services, Tacoma Narrow
Airport Manager, Renton Municipal Airport
Airport Manager, King County International Airport, Boeing Field
Senior Engineer, Boeing Corporation, Seattle

Texas
Airport Manager, City of Fort Worth Aviation Department, Meacham Airport
President, Alliance Air/Aviation Services
President, Addison Airport of Texas, Inc.
Assistant Airport Manager, Redbird Airport Management
Director and Assistant Director of Aviation, Valley International Airport
Assistant Director of Aviation, City of Brownsville Department of Aviation
Director of Aviation, City of McAllen Department of Aviation

Ms. MILLENDER-MCDONALD. Thank you. I guess that is it, Mr. Chairman. Thank you.

Mr. MICA. Mr. Ehlers?

Mr. EHLERS. No questions.

Mr. MICA. Mr. Ehlers yields to me for just a second. Let me just continue with you, Mr. Mead, on this question of the airports and contract tower airports. Were there not two studies conducted, one back in 2000 or pre-2000, of looking at those contract towers?

Mr. MEAD. Yes, we have.

Mr. MICA. And some folks were not satisfied with the results that showed that it would cost less money and actually they performed just as safe, if not safer? That was the first finding.

Mr. MEAD. That is correct.

Mr. MICA. And so we asked for another review. Is that correct?

Mr. MEAD. Yes.

Mr. MICA. Were the findings similar or dissimilar?

Mr. MEAD. They were very similar except that the cost savings had increased from the prior report.

Mr. MICA. So we would have had safer operations on that review. And not all of the 71 are in included in that category. But again, you made a determination on a smaller number that would save money and be as safe, if not safer, with that configuration.

Mr. MEAD. I would say as safe.

Mr. MICA. Would you make certain that the Member's inquiry get copies of that report.

Ms. Blakey, you are here singing the blues about money. Why have you not taken action—and we had an agreement before the last election on those towers. Why have you not taken an action to institute the changes and get those contract towers underway and save money and make them safer? You will really like that question.

Ms. BLAKEY. As we all recall, this was a matter of some controversy for the last reauthorization.

Mr. MICA. But we had a letter that was only good through the last election. Again, I know where you can save some money. I hope you take another look at that.

Ms. BLAKEY. I will take it under advisement.

Mr. MICA. Thank you for yielding, Mr. Ehlers. Did you want your time back?

Mr. EHLERS. Reclaiming my time very briefly. I would just want to reassure my good friend and colleague, Ms. Millender-McDonald, about the airports being closed from midnight to 5:00 a.m. I represent Grand Rapids, Michigan. It has a busy airport, approximately 2 million passengers a year, which puts it in a sizeable category, and that airport is closed—I am sorry, not the airport, the tower is closed during the night and it is operated out of Chicago TRACON. We have had no incidents, no particular complaints. I, myself, have flown in there with another pilot at that hour and it is handled just as if they were right there in the tower. And so, it is a safe procedure. With that, I yield back.

Ms. MILLENDER-MCDONALD. It gives me great comfort.

Mr. MICA. At great risk, I recognize Mr. DeFazio. Welcome, sir.

Mr. DEFAZIO. Thank you, Mr. Chairman. I have been here for a while. I guess we have got to back up to kind of the beginning here.

I would just like to ask each of the three panelists, is 21 percent precisely or even in any sort of calculated way the amount of operating costs of the system that should be paid by the General Fund? How do we apportion that? Why is it 21 percent? It used to be a lot more. Anybody have an idea? Have we ever done a cost-benefit analysis on what is the cost of controlling the national airspace, what is the benefit to people who do not fly but who get packages or mail that is flown, what is the cost of all the network to the business community. Have we ever looked at it in that way and said, gee, what would be a fair amount to be paid out of the General Fund, since the original idea was the General Fund would pay most everything?

Ms. BLAKEY. There have been a number of studies along those lines and I think it is fair to say that they vary somewhat. But they all point to the fact that while there is benefit, without question, to our economy and to the general taxpayer, that is usually calculated differently. For example, NCARC, the study commission that, before becoming Secretary Mineta, Congressman Mineta chaired back in 1997, suggested a figure of about 30 percent of the cost of the aviation system should be borne out of the General Fund. And that accounted for things such as you are suggesting, along with public use aircraft and military aircraft. But I would point out, at that point, they were also taking into account security, because at that point that was covered under the FAA. Now, obviously, security is a different set of costs and it is handled differently. But it was 30 percent at that point. That is one study on this.

Mr. DEFAZIO. Yes, pre-9/11. A lot of parameters have changed since then. Okay. Thank you.

Anybody else have an idea? Mr. Mead?

Mr. MEAD. Yes. The 20 percent that I quoted in the testimony, or 21 percent, is simply an arithmetic average of what has happened over the past decade. In some years, such as the last year of the last Administration, they did not tap the General Fund. But the contribution was about $3 billion in 2002-2003, and now it is around 11 percent, which would be a very low percentage.

Ms. Blakey is correct that the Mineta Commission in 1997 did posit a figure.

Mr. DEFAZIO. She said 30 percent. We will go with that for now. But my point is, it seems like kind of a departure point for this discussion about Trust Fund depletion, because that, in part, depends upon how much burden the General Fund is carrying, how quickly the Trust Fund will deplete, in addition to the other factors that have been mentioned. It seems to me that is something the Committee needs to visit and we need to have some significant discussion of, what is a proper commitment, not just under the pressures of the annual budget process, what are we going to be able to squeeze out, but what is a proper contribution from the General Fund, whether we made it an entitlement or something else. So that is one thing.

The second thing is acquisitions. Ms. Blakey, a lot of this certainly predates you. But I have been known to say that the only agency of the Federal Government worse at acquisition than the Pentagon is the FAA. I appreciate some of the earlier questions

and your testimony saying you think you are beginning to get a handle on the en route system and other parts of this. But that has been just a huge cost contributor. And if we went back to the beginning of the discussion when I came in, which is, well, gee, should we have a way to borrow money so we could capitalize things up front? If we had capitalized what was originally proposed for air traffic control, we would have a lot of junk on our hands that did not work right that we would have spent a whole lot more money for. It was not just your typical Pentagon procurement where you have something that might work and you drag it out, we had something that did not work and we had to cancel the contract, start another system, et cetera.

So I would really hope that, again, before we look at long-term commitment, substantial borrowing and funding, that we have a really good handle on the acquisitions process, which I am not totally confident we have because I hear ongoing problems. Anybody want to comment on that? Mr. Mead?

Mr. MEAD. Yes. I think that point is well taken. I would say, one, there have been a number of these big acquisitions where, frankly, the cost increases had not been communicated to the Congress or the aviation community. I give credit to Administrator Blakey and her team for recognizing that the cost of these acquisitions were much more than people were being led to believe.

Number two, there are a lot of programs that are still hanging fire. For example, STARS is one that has gone up about 194 percent in cost and has been delayed for years. The WAAS system has gone up to 274 percent and has been delayed by 12 years. So I do think there is additional work that may be done. Also in my statement I refer to support contracts.

Mr. DEFAZIO. I was going to ask a question about that. I wish you would expand on that because I thought that was a very interesting point on Page 6, where you say, over $2 billion for 100 contractors. How does government work differ from contract work done by employees at substantially higher costs to the Government? Because everyone thinks contracting out saves money. You give a specific example. Actually, I have heard from a number of people that a lot of contracting out actually does not save money but it does at least include profits. So someone makes money. Could you expand on that?

Mr. MEAD. Yes. We are very concerned about these contracts because they are not handled in a centralized way by FAA. It seems like a very large number of people can tap these contracts and just order work to be done. We have found examples where they have multiple contractors who charge multiple and different rates for the same services. We have found situations where one day a person is an FAA employee getting paid $109,000 a year, and the next day the employee is sitting in the same place, doing the same work as a contractor and the contractor is getting $206,000. This seems to be an example of poor cost control. I think FAA needs to get a handle on these contracts, handle them centrally, and perform a cost analysis before they contract out under them.

Mr. DEFAZIO. I will ask Ms. Blakey in a moment for a response, and that would be my last, Mr. Chairman. But just on that, in addition to the $206,000 cost for the former $109,000 employee, I as-

sume that we have not fully funded benefits and retirement. So we would have an ongoing cost for benefits and retirement for that employee who is now working for a private contractor at twice the cost of a full-time Federal employee. Is that correct? So maybe it would be more than $209,000 if you apportion those costs.

Mr. MEAD. Well, that would be so. I do not think that example we are using is an isolated example either.

Mr. DEFAZIO. Ms. Blakey, could you just briefly respond to that?

Ms. BLAKEY. I certainly would agree with the Inspector General that this is an area that is important for us to drill down on. We are doing that and we are analyzing specifically the contracts that he is referencing here.

I would point this out. The FAA since 1993 has dropped its total workforce by 16 percent. There was a tremendous amount of pressure both from this Congress and elsewhere to drop the full-time Federal employees, and that was done. That was accompanied, however, by the expansion of these kinds of service delivery contracts, where you are able to use the expertise of engineers, of people with tremendous experience on an as needed basis. It is certainly the case that when you use them on a spot basis, they cost more than that same salaried individual internally, but you do not have the overall carrying costs of them year-in and year-out if you are able to use them judiciously. That is the theory behind this, and certainly that has been the trend in the FAA, as I say, for more than decade.

Mr. DEFAZIO. But again, if you look at the fact that now, if that is a former FAA employee, you are having to budget for their ongoing benefits and retirement costs and the new contract which costs more. I have heard this in other agencies; it is not unique to you. And I think you are pointing out this was a stupid measure adopted by Congress and the Administration, which is let us use FTE limits as opposed to looking at how we can do things more efficiently. Just putting words in your mouth, and you certainly did not say that, for your minders who are listening. You were very good at defending the Administration here. Thank you, Mr. Chairman.

Mr. MICA. I thank the gentleman. Further questions? Mr. Costello?

Mr. COSTELLO. Mr. Chairman, thank you. I apologize, I had to duck out to go offer an amendment at a markup. My first question was just covered by my friend from Oregon, the former Ranking Member. I am glad that you had both Mr. Mead and the Administrator elaborate on the record.

In your testimony earlier, Administrator Blakey, you said that you need a consistent and reliable revenue stream. I do not think anyone would argue with that. But Mr. Mead, you have said in your written testimony that before we take action on this revenue stream and any action to change the current system as far as revenue is concerned, the FAA needs to take steps to control costs and determine future requirements before new revenue streams are explored. It seems to me that you are suggesting that the FAA needs to get their act together as far as developing plans for the air traffic control modernization and other things before the Congress

takes action as far as new revenue streams. I want to give you a chance to elaborate on that.

Mr. MEAD. Yes is the answer. I think FAA is doing a lot. The FAA today is very meaningfully engaged in cost control. I do not want to paint the picture that the glass as even approaching half empty. But I laid out four preconditions in our testimony and I think FAA can do those successfully in the next couple of years. It is almost like putting a cart before the horse in a way to talk about borrowing, adjusting taxes, or transitioning to user fees, or whatever, before FAA knows what its requirements are. But at the same time, I think it is very healthy to begin the debate now about what the implications are for these different alternatives.

Mr. COSTELLO. I think everyone agrees, including the FAA, that the FAA has over-estimated revenue into the Trust Fund. I wonder, Mr. Mead, if you have found the FAA has now taken action to correct that so that they will have better projections in the future? Obviously, the Chairman and I mentioned a number of factors as to why the Trust Fund revenue is down—9/11, the legacy air carriers reducing their prices to compete with the new entries in the low-cost air carriers. But I wonder, are you seeing progress? Do we expect in the future that the FAA will be able to give us better projections than they have in the past?

Mr. MEAD. I think they are working on it, as Administrator Blakey outlined. I would say that they are a lot better in forecasting with some precision the level of aircraft activity, but they are not as good in forecasting the level of estimated revenue.

Ms. BLAKEY. That would assume we know the future business models of the airlines as well as we know the nature of air taxis and all of these new systems coming on board. I wish we had a crystal ball. Part of this is an art, not a science.

Mr. COSTELLO. Let me follow up with you, Administrator Blakey. I think the Inspector General has pointed out that you have, in particular, made some progress in that regard and some other issues as well. But you make the point in your prepared statement that the Aviation Trust Fund is directly tied to the fortune of the aviation industry. Would that not be the same case with user fees? Would that not be directly tied to the fortune of the aviation industry just as the system is currently today?

Ms. BLAKEY. Certainly there should be a strong correlation between the services that are required and the fortune of the industry. If aviation activity dropped, presumably the costs would then drop, although it takes us a bit of time to adjust an air traffic system down. But if we assume that there is going to be increased activity, which almost every forecast I have seen says there will be, it is just the shape of that activity that is difficult to know, and to see that you need to bring the cost of the service in line with the revenues coming. Any business would run that way.

We are trying our best to run the FAA like a business. And I think it is really important to note that when you do that, the user community, the customer base, has to take into account what the services cost. That gives a much stronger set of incentives to help us control our costs and be accountable for what is really necessary and important in the system. It puts a direct link there where there is no link right now. And so we have a customer base, if you

will, that does not have to take into account in any way what the costs of the requirements are. Again, you do not run a business that. And I think we can do a lot better job of aligning those things because it provides incentives for us to control our costs that are not there now.

Mr. COSTELLO. I see my time is up. But let me ask a final question. I am looking at a publication here that I am hoping is wrong. It suggests actually that the FAA intends to dissolve the Trust Fund at the end of the current authorization in 2007. I am assuming that is incorrect, but I would like for you on the record to comment.

Ms. BLAKEY. There is a frightening thought. No. In fact, what I would say simply is this, following up on the discussion with the Inspector General, we feel great urgency because we believe that a viable, healthy Trust Fund is important. Those taxes and fees expire undeniably in September of 2007. And what we do believe is that it is certainly important for us to be able to project our costs, to have the kind of accuracy that our new cost accounting systems allow, and project the capital expenditures that the next generation system will require. But that is not, in my estimation, a rationale for us not to move forward very aggressively in this debate about what to put in place in terms of the new system, because we have no choice. If this follows the authorizations it has in the past, it will be for 10 years. And I must tell you, with the kinds of investments we are talking about, others around the world are not stopping. The Europeans, in particular, are moving ahead with capital investments and a next generation system, and that if we do not, it will leave us in the dust.

Mr. COSTELLO. Do I take that that the answer is, no, that you have not made a decision to dissolve the Trust Fund and move to something else?

Ms. BLAKEY. That is correct.

Mr. COSTELLO. Very good. Thank you. Thank you, Mr. Chairman.

Mr. MICA. Other members have questions for this panel? I have just a couple of things for the record. Nobody likes to cut and slash and save money more than me. We have eliminated some 1,400 positions, Mr. Chew testified recently, in FAA. One of the things that concerns me, as I am getting complaints about certification falling behind, Ms. Blakey, is where are we—I have got a meeting that I have asked Mr. Costello to participate with me in tomorrow—where are we on the question of adequately staffing our certification?

Ms. BLAKEY. We are concerned about this as well. We have a very strong commitment to trying to bring new products to market and to try to provide all the benefits that that does economically. But the harsh reality is that we expect this year we will be down 300 people in our safety oversight. The first priority has to be for the operational safety of the existing system. And unfortunately, the queue for those who want to bring new products to market, that line is getting longer.

Mr. MICA. Well, we are going to have to do something. With the meeting that we have tomorrow with Mr. Sabatini, we are going to have to find some solution. This Subcommittee is going to have to act. Because it begins affecting our economic base. We are losing

market share in aviation manufacturing. If we cannot provide certification services to manufacturers of equipment, it makes us noncompetitive; you become an unreliable vendor, and that is the quickest way you lose markets. So we are going to need a good analysis of what it will take, where we need to put the bucks, and how we can get us to a competitive status. So that is one question.

Dr. Dillingham, you talked about the CTI graduates, about saving money. I know we now pay people to go to school to become an air traffic controller, we pay them a salary while they are going to school. We contract all this out. We have a big operation in Oklahoma City. People who go to school end up going through Oklahoma City in a repetitive manner. Did I hear you say we could save some money? Because we are here looking at how we can make this thing work.

Mr. DILLINGHAM. Yes. The idea of allowing appropriate CTI graduates to go straight to on the job training is a way to save a significant amount of money, maybe not in the scope of $12 billion, but when you are talking about a few million dollars every year or more depending on how frequently that situation is used, it will be a part of the savings that can be obtained.

Mr. MICA. Actually, the new controllers will be earning less money, will start at a lower compensation. We have a core, in fact, our vast majority of air traffic controllers are older. Somebody handed me this earnings of various Federal employees. After Associate Justices of the United States, the top 100 FAA controllers earn an average $199,000 each. So entry level beginning would be a lot less and we are going to have a lot more folks to replace. So the more folks we replace, we would actually be saving money in salaries. The guys get pretty expensive when they hang around, do they not?

Mr. DILLINGHAM. Yes, sir.

Mr. COSTELLO. Mr. Chairman, I wonder if you might yield.

Mr. MICA. I am always willing to yield.

Mr. COSTELLO. Let me just say, and I know that you have a passion for attempting to save money whenever we can, as I do, but I think that when we are talking about the lives of the travelling public that safety has to be the number one issue. I am not disagreeing with everything you said, but I am saying that if we really wanted to save a lot of money, we could contract out the whole system and maybe—I was just in Shanghai a couple of months ago and I am sure we could get air traffic controllers from China for a dollar an hour. But the fact is that we have a responsibility to the travelling public that when they get on an aircraft that the FAA has done everything they possibly can to make certain that we have the best trained and the best, most efficient air traffic controllers and other people in the system handling their safety. We talk a lot about saving money, and I am as interested as you are in saving money, but the number one issue the public needs to understand is that we are trying to protect their safety.

Mr. MICA. I thank the gentleman. Reclaiming my time. I would agree with you 100 percent. I do not think anyone on this side has advocated hiring chinese air traffic controllers at $25 a month. But I think we can look at some efficiencies and economies, some that have been highlighted by the incredible Inspector General on sev-

eral occasions, and also GAO, Mr. Dillingham, have given us some good suggestions. And I know implementation is difficult. Ms. Blakey has her hands full and then some.

Let me yield now, if I may, to Mr. Oberstar.

Mr. OBERSTAR. Thank you, Mr. Chairman. And thanks to our panel for being very long-suffering. You have spent a long time at the witness table. That is the way it used to be around this Committee, we spent a long time in hearings where we plumbed the issues in depth, and it is important to do that.

Just a parenthetical comment on air traffic controller training. We were doing very, very well with the Twin Cities school that cost less per student compared to the Oklahoma City facility, had a greater success rate, greater retention rate, in the 90 percent range, but was cut out of the supplemental funding by the Appropriations Committee. Nothing to do with FAA or the Administration budget, just the Chairman of that Appropriations Subcommittee happened to be from Oklahoma at the time and felt that under the budget limitations it was better to shift those dollars into Oklahoma City instead of saving dollars and training more controllers, and better, at the Twin Cities facility. Nothing I did not say on the House floor, by the way, at the time of the appropriations.

Well, we are, in a sense, where we have been for the last 20 years, talking about the viability of the Aviation Trust Fund financing mechanism of a variable cost of air traffic control, what percentage of operations cost should come out of the Trust Fund and how much out of General Revenues. It is hard to pick an area that we have not already plumbed at one time or another in hearings over the last 20 years. There is, however, I think a qualitative change, not just a quantitative, but a qualitative change in the nature of funding of the Aviation Trust Fund and that is due to the consequences in aviation subsequent to September 11. Aviation changed dramatically—huge new costs were saddled on the system, travellers have changed the way they schedule their travel, how much they are willing to pay for their travel, and there has been an additional factor, which is the access through the Internet to fare selection by travellers who in some instances are able to find a lower fare on the Internet than airlines are offering on their own internal CRS. That has an affect on the revenue going into the Aviation Trust Fund.

Let me start with my pet peeve, which is that the AIP fund was raided to the tune of $1.059 billion for security in the aftermath of September 11. And PFCs paid out by airports were raided to the tune of $316 million to pay for security installations that should have come out of General Revenues. I think the General Revenue fund of the United States, defense appropriations, or whatever ought to reimburse aviation for the costs incurred to install newer, more costly security facilities at airports which aviation has diverted from capacity requirements that now are beginning to choke our airports again. I do not ask you for a comment on that, I know for Administrator Blakey, she has probably got a gag order to talk about anything like that. I know this from long experience that you are not going to comment on that, and I do not ask you to. That is something that should be done in all rightness and fairness.

What we have seen on the operations cost of things is an increase in the amount that has come out of the Aviation Trust Fund. There was a slight decline, but it went in fiscal year 2001 to nearly 83 percent coming out of the Trust Fund, it was a high of 92 percent, GAO has it somewhat higher in an estimate prepared by GAO; in 2003, it was 76 percent; in 2004, it was 78 percent, this year it is estimated at 79 percent. We used to have a figure of about 10 to 15 percent of that cost was to be paid by DoD for services provided by the air traffic control system for service to military aviation. Somewhat down because there is less military aviation. But it really raises the question, what is the threshold at which the Aviation Trust Fund should support operations which are of general benefit to the public compared to the General Fund that ought to cover such costs? Mr. Mead?

Mr. MEAD. Well, I think the best guide, as we were referring to this earlier, is the Mineta Commission report from 1997. The report discussed went into General Fund issue in considerable detail because they realized that the fluctuations in the contributions that are made by the General Fund had a big bearing on what you have to set the taxes at. Historically, over the last 10 years, it has been about 20 percent. I do not know what the magic formula is. But I think as a practical matter, it is probably a pretty heavy lift in the deficit environment that we are in to expect more than that. This year, though, the General Fund projection for 2006 is 11 percent, which is half of what the historical average has been over the past decade. So for my purposes, I guess I would take the average, say it is about 20 or 21 percent, try to work on a more scientific, deliberative way of divining what the General contribution ought to be. But I think you need one. If you are going to go down to 11 percent and hold that constant for the period of the next reauthorization, you really are talking about a pretty significant tax problem.

Mr. OBERSTAR. Yes. Now Ms. Blakey, from a policy standpoint, aviation represents 9 percent of our Gross Domestic Product, from a policy standpoint, do you not think that the General Fund ought to bear a significantly greater proportion of cost of operating the system than it does today? And what debate is there, if there is any, within the Administration or in your discussions with OMB on this subject?

Ms. BLAKEY. The discussions with OMB in terms of the Trust Fund really have not really engaged yet. Again, we are really trying to listen to the stakeholder community to explore options and really to look at this carefully and thoroughly before trying to go to specific proposals.

I can say this. That in looking at this historically, I do not think there is any question about this Administration's commitment to the fact that aviation provides a sizeable benefit to the overall economy, no question about it, and the President's budget has supported that consistently. So at this stage of the game, it is all a question of ″calculating″ the how much, because there also are other industries who contribute enormously to the economy as well where you have these same debates going on. At this stage of the game, I think what we can do is look at historically what other studies have said about what the public benefit is and try to derive

good information from that. For example, I mentioned the fact that the NCARC study said roughly their view was about 30 percent of the overall FAA operating costs should be borne by the General Fund. But that did include security. When you drill down, the latest cost allocation study in 1995 that talked about the issues of military, public use aircraft, benefits to the public such as safety oversight, certification, and those kinds of costs all lumping in, it actually came down to more like 15 percent. So there are wide variances there and I would just simply say we will do our best to study that.

Mr. OBERSTAR. I think it is important for the Administration, for certainly the OMB folks who drive these numbers, to think more substantively about the effect of aviation on our economy and what contribution the General Revenues of the Government ought to give back to aviation for the economic multiplier effect that it creates within our economy. Twenty-five years ago, that was 50 percent; that is, General Revenue paid 50 percent of those costs. And I plead guilty to ratcheting it up to 75 percent when we negotiated an agreement to eliminate the trigger that Congress had enacted, that if you do not appropriate the full amount authorized for AIP, then you cannot spend above fifty cents on the dollar for operating costs of the air traffic control system. In order to release money held back in the Trust Fund and to move ahead with a high authorization level and the PFC, we eliminated the trigger, ratcheted the contribution from General Fund up to 75 percent. But that has been a moving target ever since. We need to get some clarity on that.

One of the issues I think that airlines may reference in their testimony, I have not read it yet, is the fuel tax, the 4.3 cent fuel tax, and that this should be restored to the airlines. That generates roughly $530 million a year, for last year it was $534.3 million. What affect would there be on the Aviation Trust Fund if the 4.3 cents were repealed and returned to the airlines?

Ms. BLAKEY. Well, as I am looking at the overall allocation of fees that came into the Trust Fund in 2004, the commercial fuel tax contributed approximately 6 percent of the overall Trust Fund.

Mr. OBERSTAR. Is there a multiplier effect that would follow if that 4.3 cents were repealed, or is it just a loss of $534 million that we are not likely to make up anywhere else?

Mr. MEAD. No, it would not be made up anywhere else. I do not see how it would be. You already have a problem with the revenue being optimistically forecasted and not materializing. If you knock out 6 percent more a year, the airlines probably would like that, but that 6 percent is going to have to be made up somewhere. You can hit up the General Fund perhaps.

Mr. OBERSTAR. The ticket tax is a percentage of value, unlike the fuel tax at the pump for surface transportation. The advantage of that is in a rising economy you generate more revenues. The idea of that Trust Fund percentage tax in 1970-72, when it was established and in 1972 adjusted, was that a rising economy will provide more revenue to meet the needs of airport infrastructure. It was originally intended to be a fund for the hard side—the runway, taxiway, and the parking apron side of aviation. Then it was expanded to cover the F&E account. Then further expanded to cover

operations. What would happen to operations of the FAA if we said all those revenues just go into the hard side of aviation?

Mr. MEAD. If that happened, FAA would have to come up with another $6 billion. The General Fund, if it picks up what the President's budget is estimating, would pick up $1.6 billion. When your salaries and operations costs are exceeding well over half your budget, and your budget is $14 billion, it would definitely increase the amount that you could apply to capital and to airports. In other words, the half a billion hits that those accounts have taken would be restored and then some. You would be spending more on F&E and AIP.

Mr. OBERSTAR. And where would you get that $6 billion to spend on F&E and on operations?

Mr. MEAD. Well, you would have to hit up the General Fund, which would be general income tax dollars.

Mr. OBERSTAR. Do you think that is a possibility, Ms. Blakey?

Ms. BLAKEY. I can only look at it historically and tell you I certainly would not make that projection. I do not see anything in either the history of the use of the General Fund and the Aviation Trust Fund, over the course of 15 years, I might point out, as well as the current climate of Federal budget deficits that says the General Fund is a place that you can go for additional funding. And if you should eliminate the Trust Fund for operational costs, just this year alone you would be cutting out 63 percent of our operating budget. I would conjecture it would be almost impossible to run the system. I cannot imagine what a system would look like if we were operating on that kind budget.

Mr. OBERSTAR. From both of you a very candid, honest answer. I am sure Dr. Dillingham would concur. GAO has reviewed this for many years. What I am getting at is the range of options is extremely limited.

Mr. MEAD. That is right.

Mr. OBERSTAR. If you shifted from the ticket tax as a percentage of the value of the ticket to a fee—now we have been that road before in 1990 and 1991, revisited later in 1994-95. At that time, I characterized the ATC user fee as a cash register in the sky—you pass a certain point, ching, it goes up, you get a charge, pass another, ching, it goes up again. But is that the option for us, to ensure an increase in revenue is to tie all of the services to aviation to a precise formulaic fee-based system, that is, a charge imposed equivalent to the value of the service for which the charge is imposed? That is OMB's definition of a fee. Dr. Dillingham, what do you think about this?

Mr. DILLINGHAM. Mr. Oberstar, the questions that you are raising about the options, and the winners and losers associated with them is part of the work that we currently have underway for this Committee.

Mr. OBERSTAR. I did not like the fee idea eight or ten years ago and I do not like it much better today. But if we are going to assure the investments we need to make in the continuing modernization of the air traffic control system, then we have to think very creatively about means of financing it in addition to all the work of each of you, Ms. Blakey at FAA, General Mead, Dr. Dillingham, on showing aviation, the Congress, appropriations

committees, how to control and contain costs. But there is a point at which you still have to make those investments.

Mr. MEAD. Mr. Oberstar, we do have a problem here. There is going to be a serious mismatch between the revenues and the costs. There is a serious debate about how much the General Fund should be contributing. We cannot live with this swing of somewhere between 9 percent and 30 percent. You cannot make forecasts that way. But one thing I think would be useful. FAA has made a lot of progress since the last time you and I went around this axle on user fees. The Mineta Commission came out with its report and, you recall, it recommended cost-based user fees. Then everybody said, well, they cannot do that because they do not have a cost accounting system.

Mr. OBERSTAR. Right.

Mr. MEAD. A number of years went by, and $58 million later they almost have one. I give tribute to Administrator Blakey for that. A cost accounting system does two things. One, it tells you where you are spending your money and for what. The other thing it ought to be able to do is tell you is the cost that is being imposed by the various users on the system. Maybe in the months ahead, FAA could provide you that information plus the methodology for arriving at it. It would form a basis for discussion as to what would happen if you went down a user fee path, what would happen if you went down a tax path, what if you want to structure taxes so they roughly correlate with the consumption of use by the various users in the aviation community.

Mr. OBERSTAR. Well there are eight sources of revenue now for the Aviation Trust Fund and they are apparently inadequate in a declining fashion to support the needs of the system, even though use is rebounding and you would think that benefits also would be. The initial concept of a fee or tax would be tied to the increasing value of the system is no longer a valid concept and we have to rethink it. That is part of the work charged to GAO, and we look forward to that coming report.

Mr. Chairman, this is just the beginning and the continuation of an extensive dialogue that we have to have in a very constructive way about this most important treasure to our national economy, of all of transportation and in all the world. I keep saying this, a billion people travelled by air last year, two-thirds of them travelled in the U.S. airspace. No wonder every carrier in the world wants to get into our airspace. This is the most important airspace in the world and the most complex. The Southern California TRACON handles more operations than all of Europe combined. That is a huge responsibility. Just think of that as we go forward. Thank you very much.

Mr. MICA. I thank you. I have about forty more minutes of questions for each of you.

[Laughter.]

Mr. MICA. But I am going to let this panel go. We may have some additional questions we will submit and ask you to respond in writing for the record. Thank each of you for your testimony. We look forward to working with you as we address the challenge of funding our Trust Fund and funding the aviation system and FAA.

So thank you again for being with us. We will excuse you at this time.

I now call our second panel. The second panel consists of Mr. David Plavin, he is president of the Airports Council International-North America, and appearing on behalf of American Association of Airport Executives; Mr. James May, president and CEO of Air Transport Association; Mr. Edward Faberman, executive director of the Air Carrier Association of America; Ms. Ruth Marlin, executive vice president of National Air Traffic Controllers Association; Mr. James Coyne, president of the National Air Transportation Association; Mr. Phil Boyer, president of the Aircraft Owners and Pilots Association; and last but not least, Mr. Ed Bolen, president and CEO of the National Business Aviation Association.

I think all of you have been before the Subcommittee before. We are going to limit you to five minutes apiece. You will see the signal to stop on the timer. If you have lengthy statements or additional information you would like to have entered as part of the record, just request so through the Chair.

With those introductions, let me recognize first David Plavin, president of the Airports Council International-North America. Welcome, sir, and you are recognized.

TESTIMONY OF DAVID Z. PLAVIN, PRESIDENT, AIRPORTS COUNCIL INTERNATIONAL-NORTH AMERICA, APPEARING ON BEHALF OF ACI-NA AND AMERICAN ASSOCIATION OF AIRPORT EXECUTIVES; JAMES C. MAY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AIR TRANSPORT ASSOCIATION OF AMERICA, INC.; EDWARD P. FABERMAN, EXECUTIVE DIRECTOR, AIR CARRIER ASSOCIATION OF AMERICA; RUTH E. MARLIN, EXECUTIVE VICE PRESIDENT, NATIONAL AIR TRAFFIC CONTROLLERS ASSOCIATION; JAMES K. COYNE, PRESIDENT, NATIONAL AIR TRANSPORTATION ASSOCIATION; PHIL BOYER, PRESIDENT AIRCRAFT OWNERS AND PILOTS ASSOCIATION; ED BOLEN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL BUSINESS AVIATION ASSOCIATION, INC.

Mr. PLAVIN. Thank you, Mr. Chairman. I am here today on behalf of ACI and AAAE and we have got a written statement that I propose to submit for the record.

Mr. MICA. Without objection, your entire statement will be made part of the record. Please proceed.

Mr. PLAVIN. There is a lot of stuff in there. Thank you for having gone through most of it already today, so I will not bore you with repeating it. I did want to raise a couple of points that I thought would be useful to highlight, however.

It is obvious that everybody agrees that the Trust Fund is broken and that we need more money than the Trust Fund is now providing or that the combination of the Trust Fund and the General Fund are providing. Let me focus on airports, if I may, for obvious reasons. I am not really exactly sure why but the Administration seems to contend that $3 billion, which is a $500 million reduction, is adequate. They seem to point to the idea that there has been a reduction in their calculation of the National Plan for Integrated Airport Systems, the well-known NPIAS. ACI does a lot of work on projecting capital needs for airports, and (a) we do not think that

the NPIAS is nearly adequately reflecting the amount of AIP-eligible funding, never mind the issues relating to things that are not AIP-eligible. Our view is that it is at least 25 percent understated. But the fact is that even if you accept the $39.5 billion that the FAA projects, that still leaves you a dramatic gap, as always, between the acknowledged needs and the Federal funding level.

I am not persuaded, for example, that we have really adequately addressed the various issues. Everybody seems to agree we need more money. But at the same time, we are able to say there cannot be any more General Fund contribution, ticket taxes are bad, user fees, even if they are tied to real cost and even though actually our system is entirely reliant on user fees, are bad. It sort of reminds me of an old Monty Python routine where they sit together as the town council and decide to levy a tax on all foreigners living abroad. It strikes me that this is really what we are faced with. And ultimately, it is a political decision, in the best sense of that word, and we would be prepared to work with you to try to get to that political decision.

First, we, I would argue, should maintain the balance between the Trust Fund revenue and General Fund contributions. Unfortunately, we have depleted the Trust Fund over a long period of time, as Mr. Oberstar and Mr. Duncan pointed out, to strengthen the air traffic operations, but at the expense of its original purpose, which was to make capital investment in the system.

We believe that we need to reevaluate the roles of Government and industry, to eliminate outdated regulations both for air traffic control and for airport operations. We think those raise the cost of doing business, particularly in planning and building new capacity. We believe that permitting the establishment of a responsive operating framework can unleash innovation and save resources. And I think we need to think creatively about a broader range of options.

We should allow airports to voluntarily change their participation in the AIP program, for example, in exchange for additional financing and management flexibility. That would allow airports to operate in a more business-like fashion and to work with the FAA to provide some of the things that will be needed in order to make the system function properly.

We believe that in the short term there is some creative financing alternatives that are available that come closer to meeting the demonstrated investment needs while allowing the many partners in the aviation system, Government and private, to work out the long term fix. And we are ready to play our part in that solution.

Additionally, we believe that Congress should consider unfettering local authority for raising and using airport funding to promote better local and national solutions and potentially free resources for airports and the FAA's capital account that rely on AIP, and for airports, particularly smaller ones, that rely on AIP as their sole or near sole source of capital development funding.

We have got a number of other ideas. We have outlined them in our testimony and we would love to discuss them with you, including changes in the rules that govern airport bonds, which are the source of the vast majority of the overall capital development resources that airports use.

Finally, we believe that there is the need to look at the way users pay for the system. We have had a user funded system, we have always had a user funded system. We believe that if user funds can be more appropriately identified with the costs and the needs of the system, that could be a very positive way for the system to respond to the growing demands that everybody says are out there. Thank you, Mr. Chairman.

Mr. MICA. Thank you. We will hear now from Mr. May, president and CEO of Air Transport Association. Welcome. You are recognized.

Mr. MAY. Thank you, Mr. Chairman. You know, I was struck in preparing for today's hearing by how long we have been considering serious reform of the Airport and Airway Trust Fund and with it addressing associated FAA and air traffic management issues.

ATA has been on this issue since at least 1984. We had the Balyle's Commission in the 1990s, the Reinventing Government-USA Air Traffic Service proposal in the mid-1990s, Secretary Mineta's NCARC in 1997, and on and on. And the same message came through in each—we need to run air traffic service more like a business with a clear understanding of cost, we need to provide predictable funding with consistent with service demands, we need to provide the management tools and clear authority to get the job done, and we need accountability for performance. Lot of discussion. Lot of agreement. But little change. And that is not to say we have not made progress. AIR-21 led to the ATO. Russ Chew and his ATO team have been making some very real progress, and it has been talked about today. The very fact that they are going to be able to do a real honest to goodness cost analysis system is going to add by a factor of 1000 to this debate.

But I am a firm believer in the critical mass theory of Government. I guess that is a polite way of saying that things have to get really fouled up before we get serious about fixing them. And when it comes to Trust Fund reauthorization and the associated issues, I honestly think critical mass is at hand. For reasons I will not belabor here, the commercial passenger industry is on its back. And even the successful carriers are suffering. The Trust Fund revenues per aircraft are down, reflecting what the public is willing to pay to fly. Air traffic operations are climbing and with them delays, reflecting not simply the commercial industry's use of regional jets, but also the substantial influx of business aviation. The air traffic organization is confronting by the need for multi-billion dollar wholesale replacement, replacement of its aging and often outmoded infrastructure. Airport funding is totally out of sync with system demand. And now we are looking out to 2017 and asking this Congress how best to redesign the funding and operation of the critical infrastructure, because getting it right is essential to aviation, a cornerstone of the Nation's economy. To me, that is critical mass.

So what is it we want? We have talked about the problems. What are our suggestions? We want an air traffic organization that is run like a business, to understand its costs and to have the imperative to spend smart to improve efficiency. We want the necessary infrastructure reform to allow consolidation that will drive this efficiency while continuing to improve safety performance. We want an

air traffic control system capable of adapting to the same market forces that impact its customers.

How do we get there? Here are some principles to guide our decisions.

First, we must assure a dynamic funding stream reflecting system use through an equitable, transparent, proportional, cost-based mechanism where users pay for the service they consume. I know there is a lot of talk today about user fees. But let us be honest, this system has been funded with user fees since its inception. They may be called ticket taxes or segment fees or something else, but it is a user fee. Commercial aviation can no longer be expected to fund over 90 percent of a system cost while it is only roughly 60 percent a system user.

Second, I think you need to empower the ATO to make decisions regarding system consolidation, cost controls, productivity gains, with the understanding that business decision-makers must be held accountable. The debate over privatized towers and closing down systems overnight just on this Committee is emblematic of the kinds of political input that exists to those decisions, and you have got to give ATO the power and authority to make them, make them stick, and go forward, or otherwise we are forever lost.

Third, we need to eliminate funding and earmarks for FAA legacy programs which do not have an identifiable funding stream from the users benefitting from these programs.

Fourth, we need to distinguished between FAA and ATO programs, that includes airport infrastructure funding, which are provided for public policy purposes. Those should be funded in great part through a General Fund contribution. In contrast, services which are consumed by system users in the aviation business should be supported by those users.

Fifth, we need to think creatively about the best types of management structure for the ATO in order to enhance its management opportunities and consider, with appropriate safeguards, alternative funding mechanisms, including bonding, for long term investments.

Our bottom line is this. We can no longer expect to take billions of dollars out of the commercial airline industry to subsidize other system users or to support tangentially related public policies.

Mr. Chairman, we have the critical mass for change, and I hope this Committee will help us provide the leadership to make it happen. Thank you.

Mr. MICA. Thank you. We will now recognize Mr. Edward Faberman, executive director of the Air Carrier Association of America. Welcome, and you are recognized.

Mr. FABERMAN. Thank you. Mr. Chairman, I ask that my full comments be made part of the record.

Mr. MICA. Without objection, so ordered.

Mr. FABERMAN. Thank you. Chairman Mica, Ranking Member Costello, Congressman Oberstar, it is a pleasure to appear before you today to discuss an issue that is critical to the economic growth of communities throughout this country and the expansion of airline service. That issue is the funding of the Airport and Airway Trust Fund. This issue is essential for job and economic growth in

communities throughout the country. Therefore, it is important that we do not discourage passengers from traveling.

Secretary Mineta recently said, "Demand for low fare service is strong and growing stronger. We think that the changes underway now are the kind of market-based, cost competition that the architects of deregulation thought would happen 25 years ago." It is important that this continue. American travelers throughout this country want more service options.

It is important that all who place demand on the FAA pay their fair share of the cost they create for the FAA, and that we identify where that demand is coming from. As we consider changes to the funding mechanism for the FAA, we must also emphasize that other costs for the airline industry continue to increase. For example, security. In addition to security fees, carriers are routinely, almost on a weekly basis, asked to pay for construction to add new security equipment at airports, to add new staffing, and to do other things, including pay costs for delayed or cancelled flights because of security problems. Many of those things were supposed to have been paid for by TSA. A lot of airports in this country are collecting lower fees, lower PFCs, for example, because of fewer people traveling through those airports. Therefore, in many cases, our rentals and other airport charges are increasing. The air traffic control system is facing additional delays and congestion. These costs are also adding up.

A number of these problems are caused by an increase in the number of flights, even though many of those aircraft have fewer people on them than they have in the past. One of the comments we have heard frequently, and we have heard it today, is that due to lower fares the Government is not receiving the amount of fees and taxes as collected in the past. I would say that airlines try to charge fares that are reasonable, try to charge fares that bring in the most for them and the communities they serve. It has been an historical issue. However, I will also say that with lower fares, more people are traveling. And in many cases, we would rather have people fly four or five times a month than only fly once a month. We also note that in this economy, if you increase your fares by even 5 to 10 percent, a large percentage of people may not fly.

To allow entry and to assure the future health and growth of the air traffic control system, we recommend that future FAA and ATC funding be based on a number of principles:

One, the FAA needs to continue to take steps to reduce costs. We are convinced that under the leadership of Administrator Blakey those issues are being looked at closely. But they need to happen and they need to continue to happen.

Due to the enormous impact that commercial air service has on the Nation's economy, the General Fund must continue to help fund the ATC system. We believe that percentage should increase above where it has been in the last few years, and we think there are good reasons for that to happen.

Again, all operators must pay for the system based upon the cost they impose on the system. We note that we hopefully, I will use the word hopefully, will see general aviation even return to National Airport. However, we believe that if they are landing at Na-

tional Airport right before one of our planes, then they should contribute the same amount of money that our planes are contributing.

Finally, we think the FAA also needs to look carefully at causes of significant delays in the system. And if those delays are caused by major rescheduling, major additions in traffic, then this has to be reviewed and those who have caused those problems should also contribute more to the system.

We need to move forward with this review but we must be very careful not to block competitive opportunities. I thank you again for focusing on issues that impact true airline competition. We agree that this is only a first step and we are prepared to continuously work with you. The founders of deregulation would not have it any other way. Thank you.

Mr. MICA. Thank you. We will now hear from Ruth Marlin, executive vice president with the National Air Traffic Controllers Association. Welcome, and you are recognized.

Ms. MARLIN. Thank you. I have also submitted a written statement for the record.

Mr. MICA. The entire statement will be made part of the record. Please proceed.

Ms. MARLIN. Good afternoon Chairman Mica, Congressman Costello, and members of the Subcommittee. I want to thank you for this opportunity to appear before you today to discuss the financial condition of the Aviation Trust Fund. This is a very important issue for the future of aviation in this country.

I am Ruth Marlin, the executive vice president of the National Air Traffic Controllers Association, and I represent nearly 20,000 FAA employees across 19 different professions.

For 30 years the Airport and Airway Trust Fund has been used to fund capital improvements in aviation, investing in airports, air traffic control facilities and equipment, and research and development. This funding structure has served our Nation well and it has continued to grow with the demands placed on the system.

It is an accepted fact that while the Trust Fund revenue experienced a temporary period of decline from 2000 through 2003, that those revenues rebounded in 2004. And even the most pessimistic indicators point to continued growth in Trust Fund revenues. However, that has not stopped opponents of the current structure from attempting to manufacture a crisis.

Revenues are closely tied to the volume of air travel. They are passenger-driven. The FAA predicts a record 718 million people will travel this year and that number is expected to grow to one billion by 2015. Under the current structure of the Trust Fund, even if average air fares were only $100, the increase in the number of travelers alone would account for an additional $3 billion a year in Trust Fund revenue.

Critics of our system are quick to mention yield, seat miles, user fees, unit of production, all of these as possible revenue indicators. But NATCA believes that a critical safety function like air traffic control is better served by not attempting to obfuscate the funding discussion with corporate market choices. While more aircraft flying with more empty seats may cause yield to go down, we are not talking about leg room here. We are talking about funding our na-

tional aviation infrastructure and operating air traffic control, an essential safety function.

Ironically, the last time the Trust Fund was due for reauthorization the debate focused on addressing the increasing Trust Fund surpluses. For decades the Trust Fund surplus has been an issue of considerable controversy, leading to legislation increasing expenditures. Now, a few short years later, some Government and industry officials suggest that reducing the surplus is no longer desirable. Additionally, it is being used as evidence for their allegation that the fund is structurally deficient.

NATCA maintains that the Aviation Trust Fund surpluses have provided a valuable source of stability, allowing our national aviation investment to continue through the periods of brief revenue decline. And we made sure that program cuts were not made today that would curb tomorrow's economic growth. There have been dramatic fluctuations in the use of the Trust Fund to fund normal operations costs, and I think this morning's panel talked to that a great deal.

But NATCA is not asserting that more money is needed to fund the FAA or the operations budget. We understand the strains on the Federal budget. However, while we do not think that large increases from the General Fund are needed, we also do not believe that major cuts are appropriate. For four of the eight years since the Trust Fund taxes were reauthorized the General Fund contribution exceeded $3 billion. It is equally clear that in years where the contribution was lower it was a result of the FAA's poor forecast for Trust Fund revenue, not a desire from Congress to cut essential investment in aviation.

Fortunately, the structure of our funding mechanisms has allowed Congress to adjust the balance between Trust Fund and General Fund as circumstances dictate. Recognizing the significant national interest in maintaining and operating our air traffic control system, NATCA believes that Congress has acted appropriately in this regard. Oddly enough, the opponents of the current funding system cite eliminating the role of Congress as a reason to change to user fees. NATCA disagrees. We are talking about the safety of hundreds of millions of passengers every year, we are talking about the mobility of our nation, and an infrastructure that is a powerful economic engine. NATCA believes that the people we elect to represent us play a vital role in those decisions.

Another common argument from Trust Fund opponents is the need to replace many of our air traffic control facilities. My members work in those facilities and yes, many are in need of repair and replacement, and many projects are funded and ongoing. In the last five years, the FAA has replaced more than thirty air traffic control towers and terminal radar approach control facilities. That is an average of one every two months. Yet, to hear the rhetoric today, you would think that it is an insurmountable task, that opening a new air traffic control facility is incredibly difficult. Nothing could be further from the truth. In fact, I would argue that in the United States we have more experience opening new air traffic control facilities just in the last five years than our competitors have in their entire history.

Do we have facilities in need of replacement? Yes. Many centers are over 40 years old, just like the building we are in today. But like this building, our old air traffic control facilities are chock full of new computers, new equipment, and new technology that has allowed the workforce to do their job safely, efficiently, and more productively.

In closing, NATCA believes we should not underestimate the strength of the current FAA funding system and we should not tamper with it lightly. That Trust Fund is a stable source of revenue. We should keep it that way by rejecting radical changes based on a manufactured crisis. Thank you.

Mr. MICA. Thank you for your testimony. We will now hear from Jim Coyne, president of the National Air Transportation Association. Welcome. You are recognized.

Mr. COYNE. Thank you very much. Mr. Chairman, Congressman Costello, it is a pleasure for me to represent the National Air Transportation Association before this panel. Our association represents commercial businesses across the whole spectrum of aviation in thousands of airports across the country. We represent both the traveling passengers, air charter, flight students, maintenance companies, FBOs, many other companies that work at local airports and commercial airline airports as well. If I may, I would like to have my official statement submitted for the record.

Mr. MICA. Without objection, the entire statement will be a part of the record.

Mr. COYNE. A lot of hard work went into that. Much of it is repetitive of what has been said today, so I would like to really respond to a few of the issues that are directly related to the membership of the National Air Transportation Association.

First, I would like to sort of give a perspective about why I think we are in the mess that we are in today. As a former Member of Congress, I understand how hard it was for Congress several years ago to develop the funding strategies for the Aviation Trust Fund. And what we have developed over the years is a multiple level of revenue streams into the Trust Fund.

People talk about a predictable level, but really, no one can predict any of the various factors or parameters by which taxes are assessed. So to be secure, relatively secure, the Aviation Trust Fund relies upon different formats to collect its taxes. Of course, one format is the General Revenue Fund, another one is the ticket tax which is essentially an ad valorem tax, a function of the dollar value of the transportation provided, for airports we have funding through PFCs, a per capita tax, and we have a fuel tax. I would submit to you that the fuel tax is probably one of the most foresightful tax formats for funding the Aviation Trust Fund because it is the only format which is based upon essentially the weight of the airplane and the distance flown—the heavier the airplane, the further it flies, the more fuel is used. Therefore, we at NATA believe very strongly that the fuel tax is a very valid component and should always be a valid component of the Aviation Trust Fund funding scheme.

But here before us today is a new proposal essentially by some proponents to add a per-flight tax. All these other taxes might arguably be called user fees. But this new user fee, if you will, is so

tremendously different because it is a per-flight tax. I want to give you some indication of the impact that would have on our side of commercial aviation.

We are the commercial aviation segment which does not fly two schedules. We are the commercial aviation segment which flies to more than 5,000 airports across the country, not just 400 or 500 hundred as the airlines do. We are the commercial aviation segment which is on-demand, which flies in unusual circumstances with emergency situations, and especially in unpredictable routes and situations. Now for the airlines to propose a fixed user fee per-flight tax, it is easy for them. There are only a few dozen airlines, they will only get a few dozen bills, they know their schedules, they know where they are going to be flying. It is an easy thing for them to rely upon that tax. But for the charter industry, 2,800 different companies, flying over 1.5 million flights a year to 5,000 airports, most of the time we do not even know we are going to fly tomorrow because our passenger has not called us, and so our billing oftentimes is made several weeks after the flight. We would like to try to get it wrapped up as quickly as possible.

If the example of Europe and these other countries is to be expected, the typical user fee assessment over there for general aviation may not arrive until three or four months after the flight, and many, many of the times, I am told as much 10 or 20 percent of time, the bill is wrong. I submit to you that the Federal Government is not capable of producing millions and millions of accurate bills a year to the commuter or charter airline industry. They may think they can do it. But they have never done it. Anywhere in Government ever have we seen an example of the Federal Government sending out millions of accurate bills. And our industry is going to pay the price.

Now we happen to believe that there is a much simpler solution, which is to continue to have the fuel tax and the ticket tax in the format that it is now. I want to mention very quickly about the ticket tax. The real mess that we are in today is because we have seen about a 20 or 25 percent reduction in the average ticket price in the airlines. That has caused the average passenger payment to fall from about $12, in terms of the 7.5 percent ticket tax, to about $9. So we have lost about $3 per passenger times 600 million passengers. That is a lot of money. That same flight though, that 1,000 mile flight that we were talking about earlier today, when Congressman Hayes takes that flight he pays today with the fuel tax not $9, or not even $12 like it used to be for the airlines, he pays $60 for that same 1,000 flight in terms of the fuel tax. Furthermore, a charter operator when he flies that same flight is paying 7.5 percent of a much higher fee. The typical charter aircraft flying that same 1,000 flight will pay $450 to carry that same one passenger. So clearly, just because the airlines have seen their tax revenues fall, ours have been going up in the same environment. We have been paying more money over the last four or five years as the activity and the ticket prices in the charter industry has grown.

So we are not part of the problem. We like to think, however, that the fuel tax will continue to be part of the solution. Thank you.

Mr. MICA. Thank you for your testimony. We will now hear from Mr. Phil Boyer, president of the Aircraft Owners and Pilots Association. Welcome, and you are recognized.

Mr. BOYER. Good afternoon, Chairman Mica, Congressman Costello, and also the dedicated staff here. Like today's hearing which reminds me of a marathon, we are starting at least for me the third marathon discussion of this whole debate about how we fund the agency. And as we start this, I want you to know that we have been participants in all of the forums, all of the hearings, and will continue to be alongside the airlines and the other people represented at this table.

You have heard some testimony today and I am not going to try to get into the dollars and the numbers like our IG or like the GAO. But I would like to indicate that the Administration itself, the OMB this year has said that over the coming years, because we have had a dip in the Trust Fund, as you have heard, it will increase by the year 2010 by 53 percent. Now let us remember that this is a revenue and expense equation. So I would claim, as one of our panelist said earlier on the first panel, it "might not be as bad as painted." And just to cut to the bottom line of the written testimony that we hope will go into the record, Mr. Chairman, we look at this increase, our tried and true Trust Fund which has had its ups and downs, the General Fund contribution which I think needs to be looked at, both remain the biggest and the strongest way to fund our infrastructure.

Who do I represent? A little different than most at the table here. It is 400,000 members. Jim has members, and Ed has members, but our members are the people who fly these planes own them, the general aviation, the personal aircraft, and they are the ones that do not pass on to a customer, to a passenger in an airline, or to a business. They pay this out of their own pocket. The one thing they have told us is how they do not want this system funded. We do a lot of research. In 2005, knowing this debate was coming, we went to our membership and 96 percent oppose the use of user fees in any form to fund the system. Do not forget these also are your constituents. They are people who were here earlier today talking to this very subject on the panel. And why do they oppose? Well the great lead in, Congressman Oberstar talked about the cash register, Jim talked about how in the world are we going to ever charge for this.

[Video presentation.]

Mr. BOYER. And once again coming from this owner's pocket $71 for a short under 50 nautical mile flight, based on some rates that were projected by the Reason Foundation in 1996 when we were at the second running of this long marathon.

You know, we have looked at saving money. Here is just a few places where we have rung the cash register on the positive side, and the Administrator spoke to these. Working with general aviation, the largest user of this service, we did not come to you and say stop what may be going on. But we said, you know, there may be a better way to do this more economically. It is $2.2 billion over 10 years. How about decommissioning little used approaches, $8 million over 10 years. Or some of the tower operations overnight that are now just being looked at, $5 million over the next year.

A letter was sent to our members, your constituents, to educate them on the meetings and the things that we have gone to concerning FAA funding. We sent that actually just last month. And a quote from the letter is, we wanted to let them know it is too early to tell which way you are going, against or for a user fee system, but to indicate if you believe so, the debate develops, that this is not an option for GA. Let me just take you around the horn a bit.

A full committee chair from Alaska, as you can see, "If such a system were implemented, many private pilots would be tempted," and you heard it earlier, "to cut their expenses by 'opting out' of the NAS." Or in Congressman Oberstar's district, "I am forced on occasion to make payments on the privatized system in Canada." because they are near the border there, "I am not impressed at all. Our people and our system are really hard to beat." Or looking, Chairman Mica, at your own district, "Flying my aircraft extensively in the conduct of my medical practice and national eye research protocols, in addition to managing numerous property investments, I ask you to please exert all efforts to oppose user fees and instead support excise taxes as the way to fund our system." Congressman Costello, Illinois is not exempt from members who feel this same way. Once again, "I am encouraging you to not establish a user fee-based system to fund our system." And obviously, our own member and pilot, and we hear from him quite often in Congressman Hayes' area, and other members of the Committee, we got an equal number of letters in this way.

To sum it up. Fund the Trust Fund by excise taxes, not fees. At least 25 percent of the FAA costs should be supported by the general tax revenue. The General Fund, people did not tell, has been as high as 59 percent. There were several years it was 48-49 percent. One year only it was zero percent. General aviation is an incremental user of our air traffic system but we are committed to keeping the costs of our exclusive services very low. Thank you very much.

Mr. MICA. Thank you. We will hear from our last, patient witness, Mr. Ed Bolen, president and CEO of the National Business Aviation Association. Welcome. You are recognized.

Mr. BOLEN. Thank you, Mr. Chairman. First of all, let me ask that my written statement be made a part of the record.

Mr. MICA. Without objection, your entire statement will be.

Mr. BOLEN. Thank you. This is the first time I have had the opportunity to testify before this Subcommittee in my new capacity with the National Business Aviation Association.

Business aviation represents over 10,000 companies in the United States that utilize GA aircraft to help them compete in the global marketplace. Approximately 85 percent of the companies are small and medium size. Piston-twins and turboprops make up the majority of the business aviation fleet. Business aviation tends to fly above or below the scheduled airline service between 30,000 and 40,000 feet. We also use different airports. Business aviation operations total about 3.5 percent at the Nation's 20 largest airports.

There has been a lot of talk today about how general aviation pays. So let me be very clear about it. General aviation, all of its segments, pay 4.3 cents per gallon tax which was originally created in the early 1990s for deficit reduction purposes and later made a

part of the Airport and Airways Trust Fund. We also pay 0.1 cents per gallon for leaking underground storage tanks. Those are true of all segments of air transportation including all segments of general aviation. The operators under Part 91 pay a 15 cents per gallon tax on AvGas and a 17.5 cents per gallon tax on jet fuel. Fractional operators pay a 7.5 percent tax on their hourly charge, a $3.20 departure fee, and a $14.10 international departure fee. Charters also pay the 7.5 percent, the $3.20 departure fee, and the $14.10 international departure fee.

As I said before, and echoing the statements, the fuel tax is at the foundation of the general aviation taxes. We in this community support it strongly as the right way for us to pay our share. In terms of how much general aviation pays, when you look at the various segments of general aviation, the piston, the turbine under Part 91, the fractional operators, the Part 135 charter operations, we believe that the total amount paid into the Trust Fund from the general aviation community is in excess of $600 million.

Another question that has come up today not only is how GA pays or how much GA pays, but how much should GA pay. It has been said that general aviation represents 30 percent of the IFR traffic but pays a much smaller portion of the Airport and Airways Trust Fund revenues. GA does in fact represent 30 percent of the IFR traffic and we have looked at this according to tail numbers. Turboprops represent 7.2 percent of total IFR traffic; the pistons represent 11.2 percent of IFR traffic; and the turbojets represent 12.5 percent of the IFR traffic. Again, that is across all segments of general aviation including the fractionals and the charter operations.

Mr. Chairman, the point that I want to make here, and I want to be very clear about this, economists will tell you the percentage of the traffic one creates does not equate to the amount of cost imposed on the system. This is something that any economist will tell you. Instead, you have to look at the drivers of the cost of the system to understand the true cost imposed. If you look at some place like the Chicago area, the number of radars there, the number of controllers there, the TRACONS, those are not driven because of general aviation traffic. Those are driven because of the commercial airlines with their peak demands, sometimes operating each airline at 50 and 60 operations per 15 minute interval. We know that is true just looking at Washington Reagan National Airport where general aviation has been completely banned from the airport for the last three years and the costs associated with that airport have not gone down. In fact, when the GAO testified back in 1996, they issued a report that made it very clear that it was the peak demands of the commercial airlines that were the drivers of the cost of the system.

When you actually get to the cost imposed on the system by general aviation, I think that is an open question. But looking back at the FAA, the last time they did a cost allocation study in 1997, they suggested that GA should be responsible for somewhere in the 5 or 6 percent of total revenues.

I want to finish where a lot of people have done so today, and that is offer some guiding principles for us to keep in mind as we go through what my friend Phil Boyer described as this marathon.

The first is, do no harm. As Congressman Oberstar and Congresswoman Sue Kelly talked about earlier, the U.S. has the largest, the most complex, the most sophisticated, and the safest air transportation system anywhere in the world. We need to be very cautious before we throw out a system that has worked very well for over 35 years. We want to ensure a strong General Fund contribution, as almost everybody has testified today. We want to control the FAA's costs. We want to clearly identify the technologies needed for modernization. And, as the Mineta Commission recommended in 1997, we want to keep the general aviation fuel taxes as the mechanism through which general aviation pays. Thank you.

Mr. MICA. Thank you. And I thank each of our witnesses for your testimony today.

Let me yield to Mr. Costello.

Mr. COSTELLO. Thank you, Mr. Chairman. Mr. Chairman, as you no doubt have heard the bells, we have four or five votes on the floor. I really do not have any pressing questions. I think all of the witnesses made their points very clear. I would ask unanimous consent to keep the record open for a two week period in order for us to submit questions.

Mr. MICA. Without objection, so ordered.

Mr. COSTELLO. And I thank all of the witnesses for being here today and for your testimony. Thank you.

Mr. MICA. I also want to thank the witnesses. You represent a great cross-section of American aviation. Certainly, we do have a challenge on how we address the funding of our whole system. We have a Trust Fund that has some very serious financial problems if we continue without looking at additional means of revenue. You all represent key elements of a great system and we are going to rely on you to help us. This is sort of the kick-off of a very significant debate, discussion, on hopefully positive solutions to resolve the situation we find ourselves in.

We may submit some questions. But I want to thank you for your patience in waiting, and thank each of you for your very worthwhile testimony today.

There being no further business before the Aviation Subcommittee, this hearing is adjourned.

[Whereupon, at 1:33 p.m., the subcommittee was adjourned.]

STATEMENT OF MARION C. BLAKEY, ADMINISTRATOR OF THE FEDERAL AVIATION ADMINISTRATION, BEFORE THE AVIATION SUBCOMMITTEE OF THE COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE, U.S. HOUSE OF REPRESENTATIVES, ON THE FINANCIAL CONDITION OF THE AIRPORT AND AIRWAY TRUST FUND

MAY 4, 2005

Chairman Mica, Mr. Costello, and Members of the Subcommittee, thank you for the opportunity to discuss a topic of great importance to the Federal Aviation Administration (FAA) and to the United States of America. The financial health of the Airport and Airway Trust Fund (aviation trust fund) is critical to the stability of the airline industry and in no small part to the U.S. economy. Today I would like to provide the Committee with an overview of FAA's funding structure, which, as you know, is heavily dependent upon the aviation trust fund. I also will address the challenges that this funding structure presents and the implications for the FAA's future financial health. Without question, there is a critical need to establish a more stable funding stream for the FAA, especially in light of the turbulent business environment in which aviation finds itself.

I do not have a solution in hand today. Under Secretary Mineta's leadership, we have opened a dialogue on the future of the trust fund. At a forum between government and industry convened just last week to discuss the trust fund, the Secretary said, "We are beginning the process now, more than two years before the current authorization expires, because it is important to take the time to get the financing piece right." And therefore, I commend the Committee for holding this hearing today so that we in Government can have the benefit of a wide range of expert views and lay the foundation for change.

As this committee well knows, the FAA operates 24 hours a day, 7 days a week, 365 days a year. We run a multi-billion dollar air traffic control system that in FY 2004 served 688 million passengers and 35.1 billion cargo revenue ton miles of freight. There are FAA-operated or contract towers at 489 airports, and we are also responsible for inspection and certification of about 220,000 aircraft and 620,000 pilots. We have some 43,000 dedicated government employees working to serve the traveling public and the businesses that depend on the air transportation system. We operate and maintain a system comprised of more than 70,000 facilities and pieces of equipment. Our mission is to provide the safest, most efficient air transportation in the world, and that is what we do.

The FAA is funded by annual appropriations drawn from taxes, fees and revenue from the aviation trust fund and the General Fund. There's been a long history of funding a portion of the FAA's operating costs out of the General Fund due to recognition that aviation provides benefits to the non-traveling public and to our economy as a whole. The ratio of General Fund versus aviation trust fund financing has varied over the years. The General Fund share of total FAA appropriations has been as high as 59 percent (in FY 1984) and as low as zero (in FY 2000). The trend, however, is not in question. On average over the last 15 years, the portion of operating costs coming from the General Fund has declined steadily. In FY 2005, about 20 percent of the FAA's total budget is coming from the General Fund and 80 percent from the trust fund. Looking at the Operations account only, 63 percent of the FY 2005 appropriation is from the trust fund. In recent years, trust fund appropriations have been funded not only from the annual

revenue and interest posted to the trust fund, but also from drawing down the AATF's balance, which was over $7 billion as recently as 2001.

It might be helpful to provide a little background about the aviation trust fund. It was created in 1970 to provide a dedicated source of funding for the aviation system. Before there was a trust fund, a 5% tax on passenger airline tickets, a general aviation fuel tax, and a tire and tube tax were deposited in the General Fund. Today trust fund revenues are generated by a combination of taxes that were last authorized in 1997: a domestic passenger ticket tax of 7.5% of the price of a ticket, a domestic flight segment fee of $3.20 per segment per passenger, an international departure/arrival tax of $14.10 per international passenger, a 6.25% waybill tax on domestic cargo and mail, a general aviation (GA) jet fuel tax of 21.8 cents per gallon, a GA aviation gasoline tax of 19.3 cents per gallon, and a commercial fuel tax of 4.3 cents per gallon. The segment fee and international departure/arrival tax rates are indexed to the Consumer Price Index and have increased each year, but the airline ticket tax is a fixed percentage of the ticket price, so it is dependent on changes in airline ticket prices rather than general inflation. These taxes and fees are scheduled to expire in 2007, which also coincides with the end of the current authorization for FAA programs under Vision 100.

The problem that we faced is that the status of the aviation trust fund is inextricably tied to the fortunes of the aviation industry. The vast majority of the trust fund revenue (72%) currently comes from domestic airline passengers (with the largest portion coming from the 7.5% tax on domestic airline tickets), while the sources for the remainder break down

as follows: international departure/arrival fees (15%); commercial fuel taxes (6%); cargo waybill taxes (5%); and general aviation fuel taxes (2%). A graphic illustration of these revenue sources is shown in the attached pie chart depicting FY2004 Trust Fund Receipts. These taxes and fees are also invested by the Treasury Department in government securities and generate interest revenue for the trust fund.

Policymakers need to know that a gap that exists between our revenue and expenses, and this gap is quickly eroding the Trust Fund. From fiscal year 2001 to fiscal year 2004, the uncommitted balance of the Trust Fund dropped dramatically from $7.3 billion to $2.4 billion, as trust fund receipts were lower than predicted due to lower airline ticket prices and lower aviation demand (as a result of 9/11 and other events). In fiscal year 2006, the President's budget projects that the uncommitted balance in the trust fund will dip to approximately $1.2 billion--the lowest level in its history. This estimate is based on projected 2006 tax and interest revenue of $11.8 billion with $12.1 billion being appropriated for FAA programs. Unfortunately, over the past 4 years, our revenue projections proved to have been overly optimistic, due to the impacts of 9/11 and the unprecedented change in the structure of the airline industry. The FY2006 projected level of the uncommitted balance is sobering because it leaves only a small "cushion" in the trust fund balance. In addition, our ability to rely on an increased General Fund contribution to bridge any gap is in question due to competing budget pressures as well as the effort to reduce the federal deficit.

As we look to the future, we see a complicated and somewhat worrisome picture. We are projecting that passenger demand, which dipped severely in the wake of 9/11, will return to pre-9/11 levels by the end of this year, reaching 718 million passengers. In FY 2004, commercial operations at 17 of our 35 major airports were above pre-9/11 levels. We project that by 2006, an additional 8 will be added to that list, with some airports like Salt Lake City and Fort Lauderdale showing very high growth, in excess of 40 percent over year 2000 levels. We forecast that travel demand will continue to increase to where we could serve over 1 billion passengers by 2015.

It is very good news for the aviation industry that demand is back, but it is back in different ways than before. Domestic fares have continued to fall as a result of the growth of low-fare/low-cost airlines, changes in ticket distribution methods due primarily to the Internet, and increasing business traveler price sensitivity. It is these low fares that have helped traffic levels rebound to pre-9/11 levels. While low fares are good news for the passenger, they spell trouble for the trust fund with its heavy reliance on the ticket tax as its primary source of revenue.

Industry changes also have implications for the FAA's workload. The airlines are trying to control costs by using increasing numbers of smaller aircraft. This trend adds to the workload of air traffic controllers without increasing tax revenue commensurately. Regional jets normally carry fewer passengers than the larger airliners, so the movement toward smaller passenger aircraft contributes to the decline in the trust fund revenue per flight. If an airline carries a given number of passengers (paying the same fares) on two

regional jets instead of one larger jet, ticket tax revenue does not change, but controller workload approximately doubles. Our latest forecasts indicate that the growth in the number of smaller aircraft is expected to continue and become more pronounced. Plainly, our revenue is not tied in any way to the cost of the service, which means that there is no nexus between actual workload and how it's paid for.

Increased air traffic operations are not the only source of increased workload for the FAA. In recent years the industry has also seen more new entrant carriers. While this is good news for competition, it also has workload implications for our agency. Right now, there are 16 applications in the queue awaiting review and certification by our safety staff, and each of these new operators will bring additional pilots and crew into the system. Also, with regard to our airport grant program, Vision 100's increase in funding for the Airport Improvement Program (AIP) coupled with a new entitlement formula apportionment for non-primary airports increased our workload in processing grant applications by fifty percent.

As our workload increases and our resources are strained, we have been forced—like the industry we serve—to make changes, become more efficient and continually work hard to control our costs. As this committee has heard in previous testimony, our Air Traffic Organization (ATO) has reduced costs through productivity gains and attrition. The ATO has reduced management layers, with executive ranks reduced by 20 percent, and has consolidated a number of redundant functions, thereby reducing overhead. One example of these cost savings is that the FAA's average cost of controlling a single

Instrument Flight Rule (IFR) flight fell by 3.6% in 2004 as compared to 2003. On its own that may seem like a small figure but with more than 16 million annual IFR flights the savings add up over time. In addition, we used the competitive sourcing opportunity outlined in the President's Management Agenda, more commonly referred to as the A-76 process, for the delivery of services now provided by our Automated Flight Service Stations. This is the largest public/private competition in U.S. history. As a result, we will save the taxpayer more than $2 billion over the next ten years. Also, we are implementing a cost accounting system throughout FAA that will provide our managers and executives with the information they need to identify and eliminate wasteful spending, hold or reduce operating costs, and better link financial performance to mission objectives. Our efforts are being recognized. This month we won our second straight C.E.A.R. Award—Certificate of Excellence in Accountability Reporting. In recognition of our efforts to enhance financial management, the GAO removed the agency from its "High Risk" list.

Controlling our costs will be a major focus but we face numerous challenges in that arena. Negotiations with our major unions will begin in earnest this spring and summer. The contract with our largest union, the National Air Traffic Controllers Association, is due to expire this coming September. My goal for these negotiations with our unions is to reach new contracts that enable the agency to meet the aviation system's needs, be fair to employees and provide the flexibility that we need to operate the system. I have said before that I will not sign a contract that the agency cannot afford and I want to underscore that again here today.

An additional challenge in the upcoming years is a surge in controller retirements. We developed a plan last December for hiring and training new controllers. This plan lays out cost-saving mechanisms that will allow the ATO to reduce previous staffing projections by 10 percent over the next five years. Full implementation of the plan is under way and it will enable us to have the right people in the right places at the right time. We are also faced with an aging and deteriorating inventory of facilities and equipment. The average condition of the FAA's 21 en route air traffic control centers is poor and getting worse each year. As this Committee well knows, modernization of the air traffic control system is critical if the agency is to keep up with what aviation brings tomorrow. The price tag for these facilities and equipment alone is $2 billion per year in capital funds just to maintain current services. Given our recent F&E budgets of approximately $2.5 billion, that doesn't leave a lot of money for modernization. The total cost of asset replacement is $32 billion.

As you know from your recent hearing on our Joint Planning and Development Office (JPDO), we must also plan for the emergence of the next generation of the air transportation system. The next generation plan takes the system out to 2025, charting the course for satellite based navigation, handling new aircraft classes, on-demand services, and the increasing growth in air traffic. However, the move to a modern, efficient and technology-driven aviation system is going to require sustained, multi-year investments. As the recent flight service station A-76 experience has taught us, we will

often need to invest some money in order to make the transition to a new system that will significantly reduce operating costs and better serve our customers in the long run.

What I have outlined above—the condition of the aviation trust fund in the context of the growth in demand and industry restructuring, and the fact that FAA's future funding requirements will significantly outpace revenue from aviation taxes--clearly highlights a couple of issues. One, the current low balance in the trust fund cannot withstand a lapse in revenues. During the most recent reauthorization cycle for the current aviation excise taxes (1996-1997), Congress allowed the authority for those taxes to expire twice, which resulted in a $5 billion loss in revenue to the trust fund. We cannot afford to let that happen again. Two, the FAA needs a stable source of funding that is based both on our costs and the services we provide so that we can meet our mission in an extremely dynamic business environment. Airline ticket prices are not related to any real measure of productivity for the FAA. Regardless of how many operations we run through the national airspace system or how quickly we can certify new aircraft products and technologies, or how we continue to drive down the already low accident rate, the primary source of trust fund receipts is linked to the price of a ticket. That approach will not sustain us into the future.

Tying fees to the cost of providing service protects both FAA and the customers who use FAA services by not subjecting our ability to provide a certain level of service to unrelated factors like ticket prices. A stable, cost-based revenue stream can also ensure funding for long-term capital needs. We also believe that a cost-based revenue structure

would provide incentives to our customers to use limited resources efficiently and to the FAA to operate efficiently, as stakeholder involvement can help us ensure that we are concentrating on services that the customer wants and is willing to pay for.

I want to be clear. I am not at this point advocating user fees, or endorsing new excise taxes, or urging debt financing, or seeking a bigger share of the General Fund. There are many different ways to achieve the goal of a cost-based funding structure. I am saying that we have an opportunity in the near future for positive change and we need to begin the discussion now. Today's hearing is part of that. Also, just last week, we hosted a forum for our stakeholders to start a full debate on resource requirements and funding alternatives. We were pleased that members of your staffs were able to attend. It was a very productive conversation. As business leaders, they know that the health of the trust fund has a direct connection to the success of their industry. Our goal is to make sure that we allow for their input on this crucial issue. They responded to the opportunity with some key themes:

- *The current system is very vulnerable.* We're all aware of the uncertainties about the future shape of the aviation system – from regional jets to business jets to microjets to ticket yields. We reviewed a number of scenarios that could result in Trust Fund revenues and FAA costs continuing to diverge. To protect the system and delay the gridlock that could come as traffic increases, we need to have a funding mechanism that ensures our costs and revenues are aligned.
- While there was a clear view from stakeholders that the General Fund should continue to contribute to the FAA's budget, there was also the view that the

reality of budget deficits and increasing entitlement spending mean that *the community shouldn't see the General Fund as its salvation.*

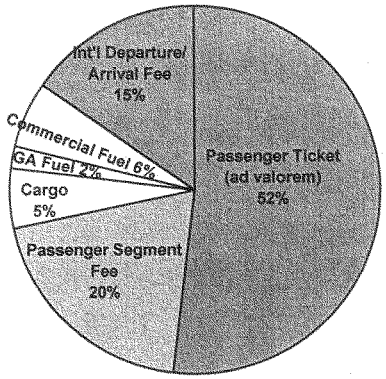
- *Any new funding system should contain the right incentives.* The system should give the FAA strong incentives to control costs and should also give users the incentives to use our limited system resources efficiently.
- *There must be equitable treatment of stakeholders.* We realize that there are many different ideas about out there about what "equitable treatment of stakeholders" means in practice - -and the devil is, of course, in the details. However, I hope that fair treatment is a basic principle that we all share as a starting point.
- *Continued consultation with stakeholders is critical in any revenue structure.*

Mr. Chairman, we will have tough decisions to make during the upcoming reauthorization of our programs, and the funding mechanism will most likely be the hardest. At this point, I see a need for fundamental change because the mismatch between the FAA's growing budget requirements and our revenue sources will hamper our ability to meet the demand for our services. In simple terms, we can't do it all and right now we can't pay for it all. Reducing needed FAA services or delaying or limiting modernization of our facilities is not an attractive option. What the solutions will be remain to be seen—after a lot of discussion and creative thinking. One thing is certain. There needs to be equitable treatment of all stakeholders. I look forward to the debate among all segments of the industry, consumers, academia, and, of course, Members of Congress. I am sure it will be a lively one.

That concludes my testimony. I would be happy to answer any questions you may have.

The majority of Trust Fund revenue comes from a 7.5% excise tax on the price of airline tickets

FY 2004 Trust Fund Tax Receipts – Estimated Allocation



U.S. House of Representatives
Committee on Transportation and Infrastructure

Washington, DC 20515

Don Young
Chairman

Lloyd A. Jones, Chief of Staff
Elizabeth Megginson, Chief Counsel

James L. Oberstar
Ranking Democratic Member

David Heymsfeld, Democratic Chief of Staff

June 16, 2005

The Honorable Marion C. Blakey
Administrator
Federal Aviation Administration
U.S. Department of Transportation
800 Independence Avenue, S.W.
Washington, D.C. 20591

Dear Administrator Blakey:

On May 4, 2005, the Subcommittee on Aviation held a hearing on the "Financial Condition of the Aviation Trust Fund: Are Reforms Needed?

Attached is a question to answer for the record. I would appreciate receiving your written response to this question within 30 days so that it may be made a part of the hearing record.

Sincerely,

Jerry F. Costello
Ranking Democratic Member
Subcommittee on Aviation

JFC:pk
Attachment

FAA RESPONSE TO REP. COSTELLO'S QUESTION FOR THE RECORD FOR THE 5/4/05 HEARING ON THE AVIATION TRUST FUND

MR. COSTELLO: Administrator Blakey, it is my understanding that the FAA is working on a cost allocation study, or a series of cost allocation studies. Please provide me with a detailed explanation of what these studies are supposed to determine. Also, when will the studies be completed?

ANSWER:

- The FAA has not done a detailed cost allocation study since 1997. Clearly there have been many changes to the FAA since then, one of the most significant being that we have implemented a cost accounting system throughout the Air Traffic Organization.

- We are currently engaged in a detailed analysis of the cost of providing services to different types of users. This study is focused on the ATO; it will take 2004 data from the cost accounting system, which is based on service delivery points (such as towers or en route centers), and distribute it to individual flights using a model developed by GRA, Inc.

- The study will then group flights according to user groups, aircraft categories, and/or types of usage, and will display each group's aggregated allocated costs. This data will enable greater understanding of what drives FAA costs.

- The cost allocation study will also facilitate comparisons of the costs users drive to the Trust Fund revenue they generate, both under the current system and under potential alternative revenue structures

- As you are aware, one of the major challenges of a cost allocation study is that a large portion of the ATO's costs are fixed, and capital assets are used to provide common services to a variety of users. Every user group claims that it is only a marginal or incremental user of the system, and the fixed and common costs should be allocated to others. There are different accounting and economic approaches to allocating these costs, and we are studying the best methodologies.

- We expect this cost allocation study to be completed by the fall of 2005.

U.S. House of Representatives
Committee on Transportation and Infrastructure
Washington, DC 20515

Don Young
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Lloyd A. Jones, Chief of Staff
Elizabeth Megginson, Chief Counsel

James L. Oberstar
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David Heymsfeld, Democratic Chief of Staff

June 3, 2005

The Honorable Marion C. Blakey
Administrator
Federal Aviation Administration
U.S. Department of Transportation
800 Independence Avenue, S.W.
Washington, D.C. 20591

Dear Administrator Blakey:

On May 4, 2005, the Subcommittee on Aviation held a hearing on the "Financial Condition of the Aviation Trust Fund: Are Reforms Needed?

Attached is a question from Rep. James L. Oberstar to answer for the record. I would appreciate receiving your written response to this question within 30 days so that it may be made a part of the hearing record.

Sincerely,

Jerry F. Costello
Ranking Democratic Member
Subcommittee on Aviation

JFC:pk
Attachment

FAA Response to Mr. Oberstar's Question for the Record (QFR) from the 5/4/05 Aviation Subcommittee Hearing on the Aviation Trust Fund

MR. OBERSTAR: Administrator Blakey, in your prepared statement you stated that a cost-based revenue structure would "provide incentives" for the FAA to operate efficiently. How precisely would a cost-based system provide such incentives? Do you envision that system users, particularly the airlines, will have greater influence regarding how and what the FAA spends on than those users currently have?

ANSWER:

- In a cost-based revenue structure, the FAA anticipates significant stakeholder involvement in scrutinizing cost accounting data, reviewing future spending plans, and developing rates for user charges. The involvement of airlines and other stakeholders who finance the system will create considerable pressure on FAA to operate efficiently and reduce costs. Congress' important oversight role must also continue in any alternative financing structure.

- If customers must pay for the services they consume, their behavior will signal what services they want the FAA to provide. This market-based information will also improve FAA efficiency by helping us to focus our limited resources on services that create value for our customers.

- Several independent studies have also addressed the concern about what cost control incentives there would be under a cost-based financing system. As Inspector General Mead pointed out in his testimony, "A positive feature of an equitable and defensible user fee system is that it should provide powerful incentives to control costs in an effort to contain increases to user fees, provided that an appropriate oversight mechanism, other than FAA, is developed. This should also translate into greater user involvement in investment decisions."

    - Mr. Mead then went on to discuss two potential oversight mechanisms—a "public interest board" of Presidential appointees without financial ties to the aviation industry and a "stakeholder board" representing different segments of the aviation industry (commercial, general aviation, labor unions, government, etc.). The NCARC report recommends the former option, while Nav Canada uses the latter. As the IG stated, the two options are not mutually exclusive.

    - Although the IG made his comments in the context of discussing user fees as a potential funding mechanism, similar oversight mechanisms could also apply to other cost-based financing systems (such as a modified excise tax structure).

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STATEMENT OF ED BOLEN

PRESIDENT AND CEO

NATIONAL BUSINESS AVIATION ASSOCIATION

BEFORE THE SUBCOMMITTEE ON AVIATION

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE

U.S. HOUSE OF REPRESENTATIVES

MAY 4, 2005

STATEMENT OF ED BOLEN
PRESIDENT AND CEO
NATIONAL BUSINESS AVIATION ASSOCIATION

Mr. Chairman, Congressman Costello and members of the Subcommittee, although I have testified before this Subcommittee on many occasions, this is the first time I have done so in my new capacity as president and CEO of the National Business Aviation Association (NBAA). I am grateful for the opportunity.

NBAA commends the Subcommittee for holding this important hearing to examine the Federal Aviation Administration and Airport and Airway Trust Fund. NBAA members have a vital interest in a strong and healthy aviation system.

NBAA was founded nearly 60 years ago to represent companies that utilize General Aviation as a tool for meeting some of their transportation challenges.

FACTS ABOUT BUSINESS AVIATION

Today, there are over 10,000 companies in the United States that utilize General Aviation aircraft to help them compete in what has become a global marketplace.

Business aviation operators encompass a broad cross-section of interests, including businesses (large, medium and small), governments, schools and universities, churches, farms, foundations, and charitable organizations.

- Approximately 85 percent of these companies are small or midsize companies--most of which own and operate a single airplane.
- Surveys indicate that 86 percent of business aircraft passengers are marketing and sales personnel, technical experts, other company representatives and customers. Only 14 percent of passengers are top company managers.
- Piston-twins and turboprops make up the majority of the business aviation fleet.
- Business aviation tends to fly at altitudes above or below the commercial airline traffic that prefers to operate in the range between 29,000 feet and 39,000 feet.
- We also tend to use different airports. In fact, business aviation represents less than 3.5% of the total operations at the nation's 20 busiest commercial airports. The ability to use these smaller, less-congested facilities is key to the value and flexibility of business aviation aircraft.

HOW GENERAL AVIATION CONTRIBUTES

Because this is a hearing on the Airport and Airway Trust Fund, I would like to spend a couple of moments discussing the various excise taxes through which the General Aviation community contributes to the Trust Fund.

General Aviation operations that are flown under FAR Part 91 are subject to three fuel taxes: 1) a 4.3 cents per gallon tax that began in 1993 as a deficit reduction tax but was later dedicated to the Trust Fund; 2) a .1 cent per gallon tax for Leaking Underground Storage Tanks (LUST); and 3) a 15 cents per gallon tax on AvGas or a 17.5 cents per gallon tax on jet fuel.

General Aviation operations that are flown under FAR Part 91(K), commonly known as fractional operations, are subject to the following taxes: 1) a 4.3 cents per gallon tax that began in 1993 as a deficit reduction tax but was later dedicated to the Airport and Airway Trust Fund; 2) LUST tax; and 3) a 7.5 percent on the airplane's hourly rate; and 4) a $3.20 segment fee.

General Aviation operations that are flown under FAR Part 135, commonly known as charter operations, are taxed in basically the same manner as fractional operations. General Aviation operations that are flown under Part 135, carrying cargo, are subject to the following taxes: 1) a 4.3 cents per gallon tax that began in 1993 as a deficit reduction tax but was later dedicated to the Airport and Airway Trust Fund; 2) a .1 cent per gallon tax for Leaking Underground Storage Tanks; and 3) a 6.25 percent tax on the cargo shipping charge.

The following chart illustrates the taxes paid by General Aviation into the Airport and Airway Trust Fund:

Part 91 Piston	Part 91 Turbine	Part 91 K Fractional	Part 135 Charter	Part 135 GA Cargo
$.043-gallon *Deficit Reduction Tax*	**$.043-gallon** *Deficit Reduction Tax*	**$.043-gallon** *Deficit Reduction Tax*	**$.043-gallon** *Deficit Reduction Tax*	**$.043-gallon** *Deficit Reduction Tax*
$.001-gallon *LUST* Tax*	**$.001-gallon** *LUST* Tax*	**$.001-gallon** *LUST* Tax*	**$.001-gallon** *LUST* Tax*	**$.001-gallon** *LUST* Tax*
$.150-gallon *AvGas Tax*	**$.175-gallon** *Jet Fuel Tax*	**7.5%** *x hourly rate*	**7.5%** *x hourly rate*	**6.25%** *x shipping cost*
N/A	N/A	**$3.20** ***passenger*** *per segment (domestic)*	**$3.20** ***passenger*** *per segment (domestic)*	N/A
N/A	N/A	**$14.10/*passenger*** *per segment (international)*	**$14.10/*passenger*** *per segment (international)*	N/A

**LUST = Leaking Underground Storage Tank*

FUEL TAXES

Although no one enjoys paying taxes, the General Aviation community has always been very supportive of the General Aviation fuel taxes.

We believe the General Aviation fuel taxes are good for the government. Compliance is extremely high because you have to pay the tax at the same time you get the fuel. And, administrative costs are extremely low. Since the fuel taxes are paid by the operator at the pump, the government does not need the army of billing agents, collection agents, auditors and dispute resolution staff that it would take to interface with thousands of General Aviation operators. As a result, amounts paid by the users go directly into the Trust Fund without large portions being siphoned off to cover "administrative costs."

We believe the General Aviation fuel taxes are good for the operators because they are easy to understand and easy to pay. There are no forms to fill out and no checks to mail. There is just a simple transaction at the pump.

We also believe fuel taxes are good public policy. The General Aviation fuel taxes measure system usage—the more a General Aviation plane flies the more fuel it burns and the more taxes it pays. These taxes are progressive in that those with a greater ability to pay tend to fly larger airplanes which burn more fuel. The fuel taxes discourage congestion since airplanes operating in crowded airspace or crowded airports are often subject to fuel-draining holding patterns or long departure lines. The General Aviation fuel taxes also provide an economic incentive for the purchase of ever cleaner, quieter, more fuel-efficient airplanes.

HOW MUCH GENERAL AVIATON PAYS

IRS records of General Aviation fuel receipts and surveys of fractional companies and charter operators show that General Aviation operations are estimated to have contributed in excess of $600 million into the Airports and Airway Trust Fund in 2004. This $600 million represents between 6 and 7 percent of the $9.2 billion collected in 2004.

HOW MUCH SHOULD GENERAL AVIATON PAY?

It has recently been suggested by some that General Aviation is not contributing its fair share into the Airport and Airway Trust Fund. The purported evidence for this allegation is the fact that General Aviation represents over 30 percent of IFR (instrument flight rules) operations but contributes a smaller percentage of revenue to the Trust Fund.

Make no mistake about it, General Aviation operations (including fractional operations and charters) do indeed represent over 30 percent of IFR operations. A breakdown of IFR activity by type of General Aviation aircraft is as follows:

Turboprops	7.2 percent
Pistons	11.2 percent
Business Jets	12.5 percent

However, as economists point out, **OPERATIONAL PERCENTAGES DO NOT EQUATE TO COSTS IMPOSED**. Economists look at cost **DRIVERS** rather than operational numbers when allocating costs.

In aviation, it is widely understood that our domestic air transportation system was designed and built to accommodate commercial airline operations. The large numbers of radars, controllers and ATC facilities in the Chicago area are NOT there as a result of the General Aviation operations in the area. That infrastructure is in Chicago in order to accommodate the peak demands of the commercial airlines at Chicago O'Hare International Airport.

The same thing can be said of any of the airports where commercial airlines operate a hub. It can even be said of those airports like Raleigh/Durham or Nashville where the commercial airlines opened hubs but later closed or reduced them.

Members of this Subcommittee who were around in 1997 will recall that representatives of the point-to-point airlines testified that the peak operations of hub-and-spoke operators drove the cost of the system to a greater extent than point-to-point operations. It was a point confirmed by a GAO report released that same year.

Mr. Chairman, General Aviation does not drive the costs of our air traffic system in proportion to the commercial airlines. **IN FACT, IF GENERAL AVIATION WERE GROUNDED TOMORROW, THE COST OF OUR AIR TRAFFIC SYSTEM WOULD NOT GO DOWN APPRECIABLY.** After all, General Aviation was grounded for a prolonged period after 9-11 and costs did not come down. Ronald Reagan Washington National Airport has been closed to General Aviation for 3 1/2 years, but the FAA's costs associated with that airport have not gone down.

The economic reality that "operational percentages do NOT equate to costs imposed on the system" is evidenced in the air traffic charges levied by foreign air traffic control entities. Much has been made of the fact that many foreign countries charge a fee for air traffic services that is "directly related to the cost of providing that service". However, in none of the countries that have been held up as suggestions for the U.S. to emulate (Canada, England, Germany, New Zealand, and Australia) are the fees based on a formula that takes total ATC costs, divides them by total operations, and applies the sum as a flat fee on all operators.

Because General Aviation operations do not drive system costs, most economists consider General Aviation to be marginal users of the system.

STATUS OF THE TRUST FUND

But Mr. Chairman and members of the Subcommittee, what is even more important than who pays what into the Airport and Airway Trust Fund is the bigger question of whether or not our nation's air transportation system will have sufficient funding to meet future demand and remain the largest, most diverse, and safest air transportation system in the world. Both as Chairman of the FAA's Management Advisory Council and Member of the Commission on the Future of the United States Aerospace Industry, I have testified before this Subcommittee on the need for an adequately funded air transportation system.

Last week, at a forum hosted by the FAA, Gerald Dillingham from the Government Accountability Office said that system funding appeared adequate through 2007 when compared to the projections Congress set forth in its Vision 100 legislation and the projections the Administration set forth in its most recent budget proposal. However, Dillingham warned that if those projections were off 10 percent, the outlook would change. At the same forum, DOT Inspector General Ken Mead questioned whether the FAA's cash flows would be sustainable over the long term.

THE NECESSARY STEPS

With FAA reauthorization coming up in two-and-a-half years, it is really not too early for Congress to begin thinking about how we should fund our future air transportation system. As you undertake this evaluation, the National Business Aviation Association urges that we keep the following principals in mind:

- Do No Harm. This principal was actually suggested by the keynote speaker at last week's Funding Forum. Today, the United States enjoys nearly 50 percent of all of the commercial aviation activity and 75 percent of all of the General Aviation activity in the world. Our air transportation system is 73% more productive and more efficient than the rest of the world's, and we have the best safety record. We need to be sure we know what we are doing before we throw away a system that has achieved such results.

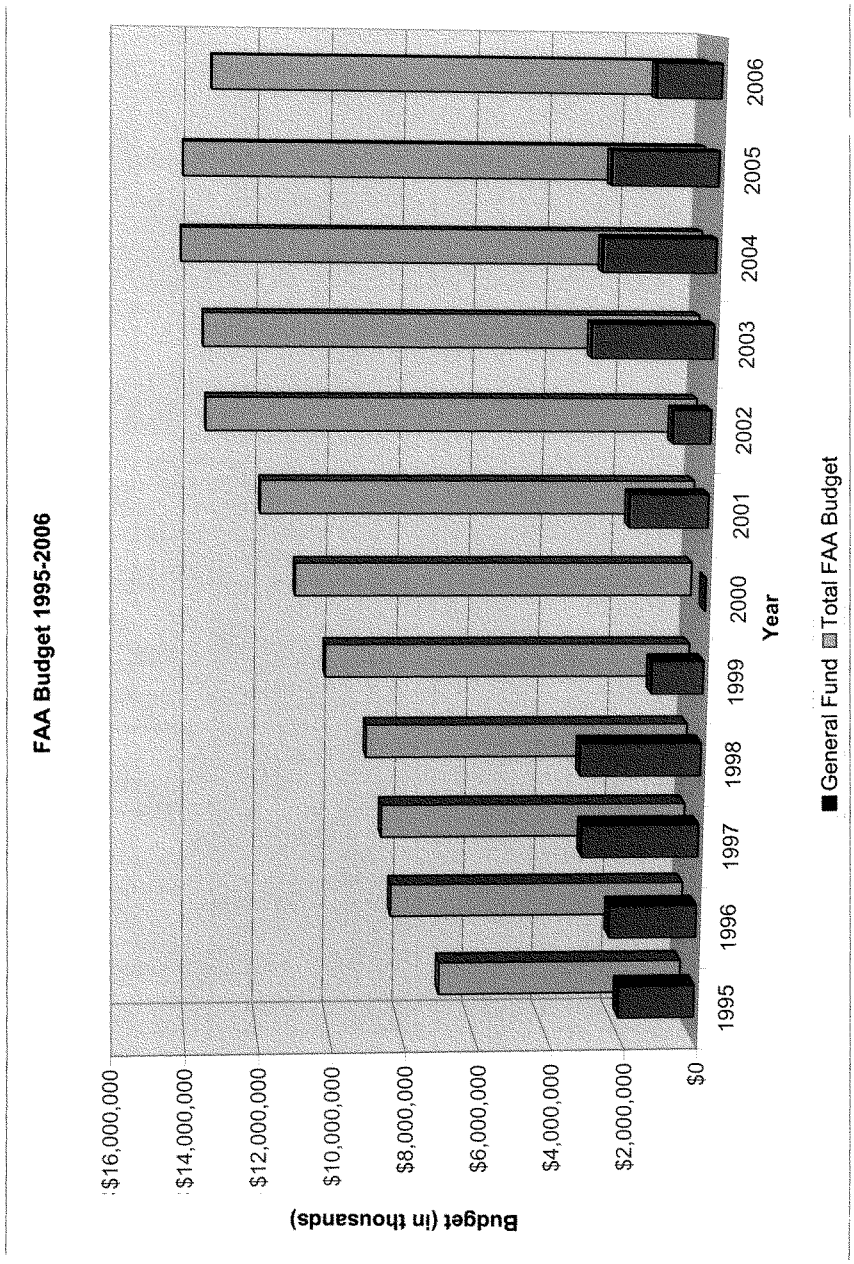
- Ensure A Strong General Fund Contribution. There is no doubt that every U.S. citizen benefits from a strong, safe and secure air transportation system regardless of whether or not they ever set foot on an airplane. As beneficiaries, the general public should continue to pay for a significant portion of our air transportation system through their general taxpayer revenues. The General Fund contribution is also necessary to cover costs imposed on the system by our military and other government users of the system.

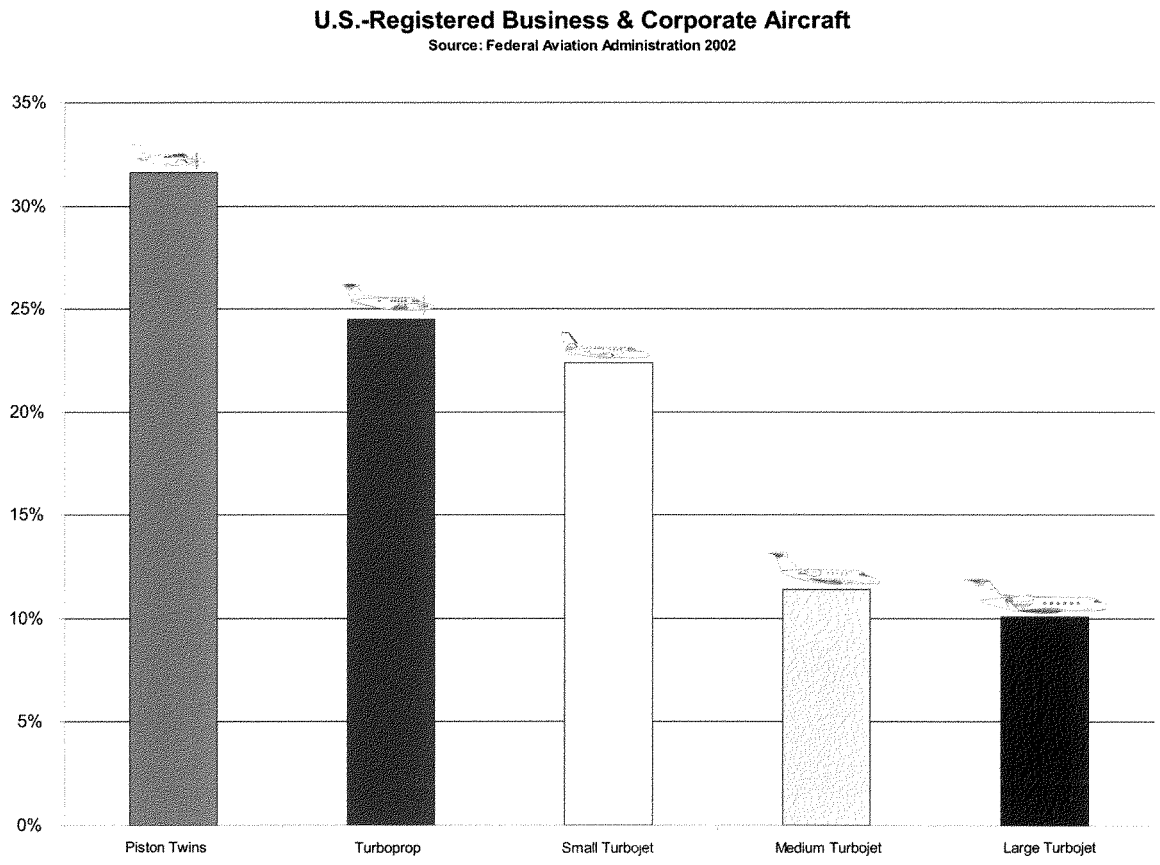
- Control FAA Costs. Over the past several years, the FAA has made tremendous progress with its costs. FAA Administrator Marion Blakey and her staff deserve a great deal of credit for their actions in this regard. However, continued progress is necessary to ensure that any additional funding, whether it comes from industry or the General Fund, is not wasted.

- Clearly Identify the Technologies Needed for Modernization. It is clear that our future air transportation system will be more satellite based than today's ground based navigation system. However, in order to get from here to there, decisions need to be made about what technologies will be used and what procedures will be adopted. These decisions and the costs related to them need to be understood and supported before we are asked to invest in them.

- Keep the General Aviation Fuel Taxes. The Report of the National Civil Aviation Review Commission which was chaired by the current Transportation Secretary, Norm Mineta, endorsed the General Aviation fuel taxes as the most appropriate way for this important segment of civil aviation to pay its share of system costs. For the reasons set forth earlier in my testimony, NBAA agrees with the Secretary's Commission.

Mr. Chairman, the future of General Aviation in the United States is directly related to the strength of our national air transportation system. We look forward to working with you and this Subcommittee to ensure that that system remains the best in the world.


FAA Budget 1995-2006
Budget (in thousands)
$16,000,000
$14,000,000
$12,000,000
$10,000,000
$8,000,000
$6,000,000
$4,000,000
$2,000,000
$0
1995
1996
1997
1998
1999
2000
2001
2002
2003
2004
2005
2006
Year
General Fund
Total FAA Budget


U.S.-Registered Business & Corporate Aircraft
Source: Federal Aviation Administration 2002
35%
30%
25%
20%
15%
10%
5%
0%
Piston Twins
Turboprop
Small Turbojet
Medium Turbojet
Large Turbojet

Top 20 Air Carrier and General Aviation Airports

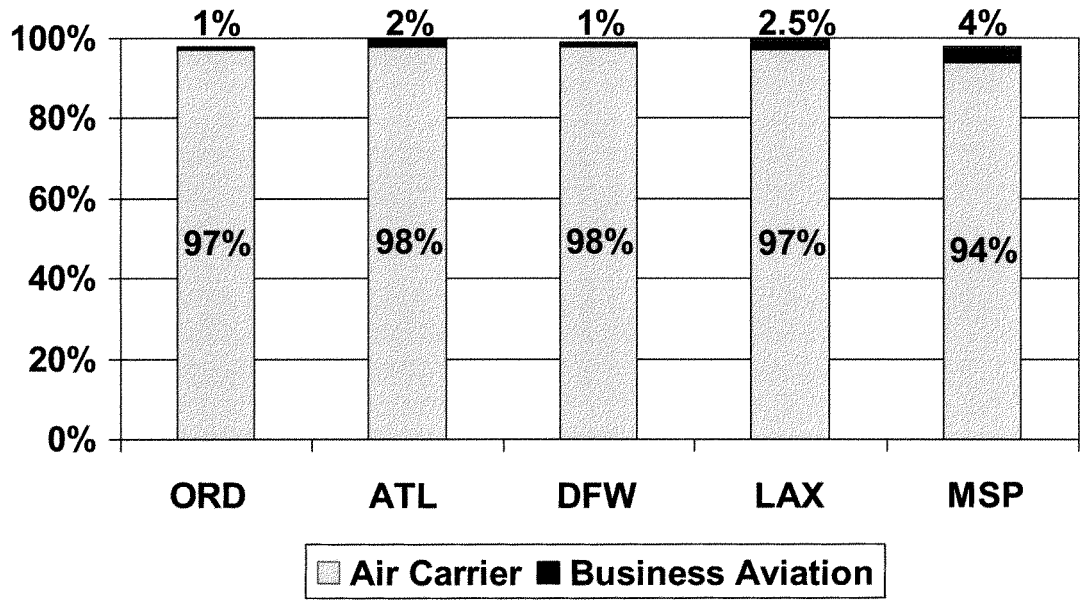
TOP 20 U.S. AIR CARRIER AIRPORTS IN 2003				TOP 20 U.S. G.A. AIRPORTS IN 2003			
Rank	Airport	State	% B.A. Ops.†	Rank	Airport	State	% A.C. Ops. ††
1	Atlanta Hartsfield Int'l	GA	1.95%	1	Van Nuys	CA	0.00%
2	Chicago O'Hare Int'l	IL	1.44%	2	Daytona Beach Int'l	FL	1.22%
3	Dallas-Fort Worth	TX	0.83%	3	Orlando Sanford	FL	1.92%
4	Los Angeles Int'l	CA	2.52%	4	Fort Lauderdale Executive	FL	0.00%
5	Minneapolis-St. Paul Int'l	MN	4.13%	5	Phoenix Deer Valley	AZ	0.00%
6	Phoenix Sky Harbor Int'l	AZ	3.33%	6	Seattle Boeing Field	WA	2.92%
7	Detroit Metro Wayne County	MI	2.52%	7	Atlanta DeKalb Peachtree	GA	0.01%
8	Denver Int'l	CO	2.37%	8	Long Beach Daugherty Field	CA	8.39%
9	Las Vegas McCarran Int'l	NV	9.92%	9	Teterboro	NJ	0.06%
10	Miami Int'l	FL	5.87%	10	Denver Centennial	CO	0.00%
11	George Bush Houston Intercontinental	TX	2.66%	11	Santa Ana John Wayne	CA	23.76%
12	Newark Liberty Int'l	NJ	1.96%	12	Tulsa Riverside	OK	0.00%
13	John F. Kennedy Int'l	NY	1.62%	13	Mesa Falcon Field	AZ	0.11%
14	Philadelphia Int'l	PA	7.72%	14	Morristown	NJ	0.00%
15	San Francisco Int'l	CA	7.35%	15	San Diego Montgomery Field	CA	0.00%
16	Memphis Int'l	TN	6.46%	16	La Verne Brackett Field	CA	0.00%
17	Orlando Int'l	FL	4.44%	17	Carlsbad McClellan Palomar	CA	0.00%
18	Baltimore-Washington Int'l	MD	7.17%	18	Chicago Palwaukee	IL	0.00%
19	Seattle-Tacoma Int'l	WA	1.77%	19	San Antonio Int'l	TX	24.35%
20	St. Louis Int'l	MO	2.53%	20	Dallas Love Field	TX	34.31%

† % Business Aviation Operations

†† % Air Carrier Operations

Source: FAA

Business Aviation Activity at the Nation's 5 Busiest Airports



Source: FAA, 2003 Activity

REMARKS OF CONGRESSMAN BOSWELL
AVIATION SUBCOMMITTEE HEARING ON THE
CONDITION OF THE AVIATION TRUST FUND
MAY 4, 2005

Given the precarious condition we find our nation's airline industry, this is an important and timely hearing to examine the condition of the Aviation Trust Fund. It is important for us to take a moment and determine where we've been, where we are, and where we are going with our aviation system. I, like many members of this Subcommittee, are strong proponents of our nation's aviation infrastructure. To maintain our first-rate system, adequate resources must be available.

Some have raised concerns about the future and how we can maintain FAA operations and capital investments with our present funding situation. The shrinking discretionary portion of the federal budget raised great concern about our ability to maintain existing FAA operations and capital improvements. There has been some discussion, and fortunately it has been minimal, of raising user fees on aviation users ---- both on passenger and general aviation. In my opinion, this would be not only unwise, but harmful to our aviation system.

With our nation's airlines already hemorrhaging red ink, any additional fees would certainly hasten their demise. As a strong proponent of general aviation, and a pilot myself, I maintain our GA users already pay a fair share for their use of the system. I would strongly oppose any effort to change the fee structure already in place.

We need to examine how the present trust fund, in combination with federal funding from the general fund, can meet our current and future expenditure needs. We also need to determine what vision the FAA has for our aviation system. This is a critical component to see how sufficient our trust fund expenditures will be in meeting our current and future obligations.

Aviation is a vital component to our nation's economy and we need to do all we call to see it expand and prosper. I, along with a number of my colleagues, look forward to hearing today's witnesses and see how we can best address our aviation system's needs. Thank you.

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Statement of Phil Boyer

President

Aircraft Owners and Pilots Association

before the

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE
AVIATION SUBCOMMITTEE
U.S. HOUSE OF REPRESENTATIVES

The Honorable John L. Mica, Chairman
The Honorable Jerry F. Costello, Ranking Member

concerning

Financial Condition of the
Aviation Trust Fund

May 4, 2005

Good morning, my name is Phil Boyer, President of the Aircraft Owners and Pilots Association (AOPA) representing over 400,000 pilots and aircraft owners -- more than half of all the pilots in the United States. Because AOPA has members in every Congressional district in the country, I appear before you today expressing the views of your constituents who belong to AOPA. AOPA members recognize the important role of the Federal government in aviation policy and are extremely involved in the democratic process with 94% voting in the 2004 election, compared with the national average of 55%.

AOPA members are involved in personal and business aviation, the majority using their aircraft in the way you use your personal automobile. These individual pilots are the only segment of aviation to pay for the aviation excise taxes out of their own pockets and are very interested in the discussion currently underway on the future of funding the Federal Aviation Administration (FAA).

I would first like to thank the Chairman for holding this hearing today. The Airport and Airway Trust Fund, known as the Aviation Trust Fund, plays a critical role in ensuring a safe and efficient aviation system for all users of the National Airspace System (NAS).

The Current System has Weathered Difficult Times, but Works Well

The United States moves more general aviation pilots, commercial aircraft and goods through our air traffic control system then any other country in the world, and we do it well. As this committee has heard, the U.S. Air Traffic Control system handled over 159 million operations in 2000. The next five largest systems combined only handled 12 million operations in that same year.

Since this hearing is titled "Financial Condition of the Trust Fund," I'll start by reporting on the status of the fund. According to the President's FY2006 Budget, the Office of Management and Budget (OMB) projects the government receipts into the Aviation Trust Fund to grow from the $9.2 billion of today, to $14.1 billion by 2010. This represents an increase of 53%.

Despite what some have argued, this leads us to conclude that the Trust Fund has come through some difficult challenges in the past few years, with September 11 at the top of that list, but its revenue numbers are strong and look to continue growing in the future. However, as we all know, the balance of the Aviation Trust Fund is determined not only by the revenue, but also by the expenses.

AOPA is concerned that the Administration has proposed increasing the expenses drawn from the Aviation Trust Fund, and decreasing the amounts drawn from the General Fund to pay for the FAA's budget. AOPA strongly objects to this artificial funding crisis by drawing down the Aviation Trust Fund in this manner.

The FAA can and must live within the revenue paid by taxpayers. With OMB's 50% increase in revenue predicted for the Trust Fund and a strong commitment of resources from the General Fund, the Aviation Trust Fund should remain a strong and stable source of funding for FAA infrastructure.

Excise taxes on aviation fuel are the appropriate way for general aviation to help pay for the aviation system, not user fees.

AOPA members, your constituents, are strongly opposed to a user fee funded aviation system. The current excise tax on aviation fuel is an equitable measure of general aviation's use of the National Airspace system because fuel consumption directly relates to operating the aircraft. Here is a sampling of what AOPA members have to say on the subject:

"I believe that this excise tax is a win-win situation – it is efficient for the federal government to administer, it helps pay for the NAS even on those flights when I don't use any of its services. I am very concerned about the negative effect that a user fee based system would have on aviation safety. If such a system were implemented, many private pilots would be tempted to cut their expenses by 'opting out' of the NAS, i.e., avoiding discretionary use of FAA-controlled airspace and avoiding the FAA flight service system."

Paul R. Larson, Anchorage, AK

"I am forced on occasion to make payments on the privatized system in Canada. I'm not impressed at all. Our people and our system are really hard to beat. I hope we don't destroy something as good as this in the name of privatization."

Gerry Robbins, Pine City, MN

"I actively use the US airspace system flying my aircraft extensively in the conduct of my medical practice and national eye research protocols, in addition to managing numerous property investments across the country. I ask you to please exert all efforts to oppose user fees and instead support excise taxes as the way to fund our aviation system."

William J. Dunn, MD, FACS, CHE, Florida Retina Institute, Daytona Beach, FL

"I am encouraging you as a member of the House Sub-Committee on Aviation to oppose any efforts to establish a user fee based system to fund the FAA Air Traffic Control system."

Bernard A. Paul, Attorney at Law, Marion, IL

"I am generally of the strong opinion that too much government is not a good thing, but there are some things, in my opinion, that the federal government should control. The air traffic control system is one of those things."

Richard P. Baxter, President CRS, Monroe, NC

"Without the benefits of the FAA system as presently configured, I would not be able to conduct and grow my business. In fact, if additional costs were imposed on the use of my airplane through a user fee-based system, it would limit severely our ability to grow and ultimately our ability to survive."

Emmanuel Daskalakis, Aralia Olive Oils, Cambridge, MA

Aviation is not alone in its use of excise taxes as an important method of raising revenue for infrastructure projects. The highway tax is virtually identical in its structure and effectiveness. For the millions of automobile drivers on the nation's highways, to the hundreds of thousands of pilots flying general aviation aircraft, excise taxes simply make sense as a safe, efficient and fair method of tax collection system.

There are also concerns that assessing user fees for air traffic services denigrates safety by discouraging aircraft operators from using the services. For years, AOPA has worked with the FAA, through our Air Safety Foundation to continually lower the accident rate for general aviation. A piecemeal system of fees and charges gives pilots a direct financial incentive to avoid using the safety features and programs provided within the National Airspace System. It would be counter intuitive to allow the FAA to shift to a user fee funded system after general aviation has had the lowest number of accidents and the lowest accident rate since 1938.

Finally, collecting the current aviation excise taxes is extremely efficient with a low cost of collection and has been in place for over three decades. During the last debate on aviation taxes and fees in the late 1990's, the Internal Revenue Service reported that it only cost $1.7 million to collect over $5.5 billion in excise tax revenue. A mere .001% cost by the government to collect! Collecting user fees would require a huge new accounting bureaucracy with a much higher cost to collect the fees because of the complexity of such a system. The reality of such a system is more money would need to be collected simply to break even.

However, it is not just about how much the aviation industry pays to support the FAA.

The air transportation system is vital to the United States economy and at least 25% of the costs to fund the FAA should be supported by general tax revenues. All citizens benefit from a safe and efficient system of air travel.

When Congress created the Airport and Airway Trust Fund in 1970, it did not expect the trust fund to finance FAA's entire budget. A contribution from the general fund was assumed. However, the amount of general fund contribution has decreased dramatically over time.

As the following chart illustrates, in the 1980's - the general fund contributed to about 45% of the FAA's budget. By the end of the 1990's, this had decreased to 29%. For the last five years, the general fund support has ranged from 0% to 24%. Considering the importance of a healthy aviation system to the nation and the role FAA plays in national security, this wide variation in support should not be allowed to continue and a 25% general fund contribution to the FAA's spending should be established.

According to the FAA, general fund contributions in the last 10 years –

Year	$ General Fund	% of FAA's Budget
1995	$2,122,000,000	26%
1996	$2,420,000,000	30%
1997	$3,255,000,000	38%
1998	$3,351,000,000	37%
1999	$1,474,000,000	15%
2000	0	0%[1]
2001	$2,129,366,000	17%
2002	$1,104,229,000	8%
2003	$3,244,588,000	24%
2004	$3,010,206,000	22%
2005	$2,827,809,000	20%

The general fund contribution is a critical component in allowing the FAA to successfully plan for long-term capital improvements. The general fund ensures that the top-line budget of the FAA can remain strong through unforeseen difficulties for commercial or general aviation.

The FAA and the aviation community should identify areas for cost savings by eliminating FAA services no longer needed and developing alternatives that save money and improve the quality of other services where possible.

AOPA has shown a commitment to reducing the costs of services utilized by the general aviation community and at the same time look for ways to improve safety by enhancing the quality of FAA services.

Flight Service Station Modernization -

For years AOPA has worked with members of this Subcommittee to modernize and improve the important services provided by the dedicated FAA employees of the nation's Flight Service Station (FSS) system. These 61 FSS facilities provide important weather and safety of flight information to general aviation pilots. As early as 1999, it became apparent to us that changes were needed to modernize the system and reduce the cost of providing the service. In

[1] The authorization had expired so there was no formula in law requiring a general fund contribution.

surveys and discussions with AOPA members, the overriding concern was their belief that the federal government has a responsibility to provide this service without a user fee.

With this as the background, AOPA worked as a party of interest throughout the development of the A-76 outsourcing study initiated by the FAA in 2002. The AOPA staff focused on ensuring that the bid criteria had appropriate requirements for the vital safety and service functions performed by the FSS. Congress supported this in direction offered by the House Transportation Appropriations Committee in its report on FY05 funding (House Report 108-671).

Competitive sourcing for flight service stations. *—In order to maintain a high level of safety and efficiency in the provision of flight service activities, the Committee urges FAA to ensure that the flight service station competitive sourcing effort require bidders to provide comprehensive and specific customer service standards for providing flight briefings to pilots as well as a process for ongoing customer service monitoring and evaluation.*

In February 2005, the FAA announced that Lockheed Martin with its FS21 proposal won the $1.9 billion ten-year contract. This proposal is designed to save taxpayers $2.2 billion over this ten-year period. But it is not just about saving money, the FAA and Lockheed Martin promise dramatic changes for pilots through call center standards and other performance based criteria.

Thus far, AOPA members have responded with enthusiasm for the new system because telephone briefings and all of the in-flight radio frequencies will continue being available. But in the future, pilots will also be able to get an interactive briefing and see the same charts and weather maps on the computer as the briefer. Lockheed's plan is to eventually consolidate the current 58 automated FSS facilities in the lower 48 states, Hawaii, and Puerto Rico into 20 facilities. All the FS21 facilities will be tied together in a network, sharing a common database and briefers will be trained to specific geographic areas, ensuring pilots will still have access to specialized knowledge of local conditions.

While AOPA does not support outsourcing of core air traffic services, the FAA chose this approach to address FSS and AOPA worked closely to ensure services would improve for pilots. AOPA staff continues being involved to hold the FAA and Lockheed Martin to their commitments for modernization and improvements in services.

Eliminating Redundant Ground Navigation Aids -

The FAA recently announced in a Federal Register notice and sent letters to 430 airport managers regarding the elimination of underutilized Non Directional Beacon (NDB) approaches. This technology is based on AM radios and has been in use since the 1930's. AOPA helped educate pilots about the possible cancellations and is working with the FAA in gathering feed back from pilots to ensure that cost savings can be achieved by eliminating redundancies, while protecting ground-based navaids in critical locations.

Cost savings for each NDB approach is $17,000 to $19,000 per year. In this initial phase, the savings are achieved through eliminating the approaches, while additional savings in equipment will likely take place in future years.

Nighttime Closure of Low Volume Towers –

As many of the members of the Subcommittee are aware, the FAA is reviewing a list of 48 towers for a potential reduction of services. The FAA estimates savings from this measure will be around $100,000 per year for a total reduction of nearly $5 million per year.

This issue highlights one of the underlying realities of the National Airspace System and its costs. Most of the features of the current system have been designed for commercial aviation. In particular, many of the major infrastructure components that have been pointed out throughout this debate as crumbling and in need of major, expensive repair were designed primarily with commercial passenger service airlines in mind. A National Airspace System designed solely for general aviation would look vastly different and cost much less than the current system.

AOPA members successfully and safely fly every day at airports without a tower. While we appreciate the additional safety provided by an air traffic control tower, the vast majority of the 19,000 airports and landing facilities in this country do not have towers.

In situations where there is a low volume of air traffic, a reduction in hours may offer savings in the FAA's budget. The Association will make members aware of potential tower closings and will provide any comments from members to the FAA for evaluation of local facilities.

Wide Area Augmentation System (WAAS) landing systems –

AOPA has not limited its cost cutting recommendations to current systems, but also to advocating for more cost-efficient systems for the future. The use of the Global Positioning System as a primary navigational aid will lower the ongoing operational costs for the FAA.

GPS has benefited many sectors of the U.S. economy. The Wide Area Augmentation System (WAAS) augments the GPS signal to provide very accurate positioning information. This new WAAS system has conveyed many benefits for agriculture, maritime industries, railroads, homeland security, enhanced 911 calling systems, earthquake and volcano warning systems, and, of course, aviation.

Through the use of the WAAS system, the long-term cost of providing instrument approaches to all 5,400 public use airports in the country drops significantly.

The cost to provide the WAAS signal is just under $50 million per year. This signal can serve all 5,400 public use airports. Current ground based systems like the traditional Instrument Landing System (ILS), cost over $82 million in annual maintenance at the 600 ILS airports.

Since there are no ground navigation systems to purchase or maintain, the cost of installing a WAAS approach is less than 10% of an ILS. In addition, the annual maintenance costs can be as high as $85,000 for a typical ground based system; the cost to maintain a WAAS approach is less than $3,000 every two years.

AOPA supports moving towards more satellite based navigational systems in order to lower the operational costs of providing navigational assistance. AOPA supports the WAAS program and encourages its future deployment.

The FAA and the aviation community should help develop the design and determine the cost for modernizing the air traffic control system

As the Subcommittee heard in its recent hearing on the Joint Planning and Development Organization (JPDO), the FAA in conjunction with other government agencies and the aviation industry is developing the year 2025 ATC system. This long-term effort is augmented by the ten-year outlook known as the Operational Evolution Plan (OEP).

While the FAA has conducted a forum on the Agency's funding, it is apparent that the FAA's modernization plan must be developed so that Congress, the executive branch, and the aviation industry have an understanding of what is anticipated for the future. Absent that, the FAA can only offer warnings about the need for capital investments without any specifics on the system and funding required. The lack of design details and costs of the future system create serious challenges for everyone involved in aviation. It places AOPA in a position of being unable to even conduct rudimentary analysis to determine what it means to our members.

The FAA and the aviation community should explore innovative approaches to financing capital improvements.

As the aviation community and government evaluate the FAA funding and modernization issues, one area that should be considered is ideas for obtaining the investments in capital improvements. The federal budgetary requirements under the "pay as you go" approach limits significant capital investments in a one-year period. This is especially true during times of budget deficits. While it is unclear how this will impact timing of future FAA purchases, there are ideas that should be explored including leasing, vendor financing and other options to provide the needed capital purchases. While the Association supports analyzing these options, AOPA members would not support a financing approach that requires user fees.

Conclusion

Thank you for the opportunity to provide AOPA's perspective on issues associated with FAA's funding. To reiterate, AOPA's position on the FAA Funding Issue:

- Excise taxes on aviation fuel are the appropriate way for general aviation to help pay for the aviation system, not user fees.
- The air transportation system is vital to the United States economy and at least 25% of the costs to fund the FAA should be supported by general tax revenues.
- The FAA and the aviation community should identify areas for cost savings by eliminating FAA services no longer needed and developing alternatives that save money and improve the quality of other services where possible.
- The FAA and the aviation community should develop the design and determine the cost for modernizing the air traffic control system. The FAA and the aviation community should explore innovative approaches to financing capital improvements.

AOPA appreciates the opportunity to testify and looks forward to working with the members of the committee as future policies for the FAA are developed.

Congressman Russ Carnahan (D-MO)
House Transportation Committee
Aviation Subcommittee
Hearing on the Financial Condition of the Aviation Trust Fund
Opening Statement
April 20, 2005

- Thank you, Mr. Chairman.

- The U. S. relies on the Aviation Trust Fund to maintain the quality of our airports and airways. We also rely on the Aviation Trust Fund to fund FAA programs.

- Recent revenue forecasts for the Aviation Trust Fund have been overly optimistic. These erroneous forecasts, along with changes in the aviation industry, have led the Administration and the FAA to begin consideration of alternative ways to finance the nation's aviation system.

- As this Subcommittee continues to look at the myriad challenges facing aviation in the United States, the condition of the Aviation Trust should be examined closely.

- I thank the Chairman and the Ranking Member for holding this hearing, and I look forward to hearing testimony from the witnesses today.

OPENING STATEMENT OF
THE HONORABLE JERRY F. COSTELLO
AVIATION SUBCOMMITTEE
FINANCIAL CONDITION OF THE TRUST FUND: ARE REFORMS NEEDED?
MAY 4, 2005

- Thank you, Chairman Mica for calling today's hearing on the financial condition of the Aviation Trust Fund.

- Regardless of the varying opinions about the future of the Trust Fund, **there is no disagreement that the Trust Fund's uncommitted balance has declined over the last few years.** At the end of fiscal year 2000, the Trust Fund's uncommitted balance was a little more than $7 billion. At the end of fiscal year 2004, the Trust Fund's uncommitted balance was roughly $2.45 billion.

- As the Inspector General will testify today, Trust Fund revenue estimates for the last few years have been overly optimistic. For example, for fiscal year 2004, the actual receipts plus interest credited to the Trust Fund was 12% less than projected. The shortfall between projected revenues and actual revenues has been made up from the Trust Fund's uncommitted balance. A major question before this Subcommittee today is – *are the FAA's revenue projections reliable?* To its credit, the FAA has initiated an independent review of FAA's aviation activity and revenue forecasting methodologies.

- The downturn in passenger travel associated with the September 11th terrorist attacks clearly depressed Trust Fund revenues.

- There are also indications that underlying structural changes within the airline industry are affecting Trust Fund revenues, as well as the FAA's ability to forecast those revenues. For example, it has been widely suggested that the growth of low-cost carriers and corresponding fare reductions by legacy carriers have driven down passenger ticket tax returns that account for roughly 50% of annual Trust Fund revenue.

- The FAA is currently predicting that Trust Fund revenue will increase over the next few years. Yet, even with this increase, FAA believes that

revenues will be less than were forecast when Vision 100 was enacted in 2003.

- The Government Accountability Office (GAO) will testify that if revenues are 10% less than now projected, under current law, the Trust Fund's uncommitted balance would reach zero by 2007. If traffic is less than expected, or fares drop, we will need to consider measures to address the shortfall, which could include cutting the FAA's programs, raising taxes, or obtaining a larger general fund contribution.

- As to the possibility of cutting the FAA's programs, last month the Inspector General testified before this Subcommittee that we clearly cannot continue to cut the FAA's capital budget and still technologically "transform" the national airspace system for the 21st Century.

- Regarding the general fund contribution, I still strongly support the mechanisms Congress enacted in AIR-21, particularly the guaranteed funding provisions and the Trust Fund and general fund contribution formula. The FAA's programs should be fully funded at their authorized levels and if Trust Fund revenues fall short the general fund should contribute whatever it takes to meet the authorized levels.

- Mr. Chairman, some have suggested that we need sweeping reform of the current aviation tax system, such as the wholesale adoption of a cost-based user fee. **While I am open to all ideas, I think the idea of switching to a user fee system raises more questions than answers.** For example, I do not understand how a user fee will generate more revenue than the current system unless the aviation community in the aggregate would pay more than it does now. To raise more revenue, someone will have to pay more.

- Additionally, some have suggested that Congress ought to consider alternative financing mechanisms such as bonding. However, before Congress considers bonding authority, the FAA should explain precisely what it would purchase with this authority. Further, proponents of bonding need to provide more information of how this authority will impact the federal discretionary budget.

▷ Thank you once again, Mr. Chairman, for holding this hearing. I look forward to hearing from our witnesses.

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NATA
National Air Transportation Association

Statement

of the

National Air Transportation Association

before the

Subcommittee on Aviation,

Committee on Transportation and Infrastructure,

U.S. House of Representatives:

Hearing on

The Financial Condition of the Airport and Airway

Trust Fund

May 4, 2005

2167 Rayburn House Office Building
Washington, DC

Appearing for NATA:
James K. Coyne, President

Chairman Mica, Ranking Member Costello, and Members of the Subcommittee:

Thank you for this opportunity to appear before you to discuss the financial condition of the Airport and Airway Trust Fund. My name is James K. Coyne, and I am president of the National Air Transportation Association (NATA). NATA, the voice of aviation business, is the public policy group representing the interests of aviation businesses before the Congress, federal agencies and state governments. NATA's over 2,000 member companies own, operate and service aircraft and provide for the needs of the traveling public by offering services and products to aircraft operators and others such as fuel sales, aircraft maintenance, parts sales, storage, rental, airline servicing, flight training, Part 135 on-demand air charter, fractional aircraft program management and scheduled commuter operations in smaller aircraft. NATA members are a vital link in the aviation industry providing services to the general public, airlines, general aviation and the military.

The Airport and Airway Trust Fund is the lynchpin of America's air transportation system. Since its creation in 1980, the trust fund has provided billions of dollars for aviation infrastructure development that has truly made the United States airspace a nationally integrated system. Thanks to the leadership and foresight of this Committee, in recent years Congress has taken extraordinary measures to unlock the potential the trust fund holds for the aviation industry. Landmark legislation such as AIR-21 and Vision 100 have ensured the integrity of the trust fund and guaranteed that the revenues that air travelers pay into the system are used solely for improvements to aviation infrastructure.

In the past few years, however, the trust fund has seen a decline in revenues and balances. The September 11, 2001 terrorist attacks and the ensuing economic downturn have had a devastating effect on the aviation industry. Fewer air passengers, reduced schedules, and lower fares overall have combined to drive trust fund revenues down. However, despite the many challenges the industry faces today, including soaring fuel costs and burdensome and often unnecessary security requirements, the industry is regaining strength and is back to the levels of air traffic we saw in the years leading up to 9-11. This summer looks to be one of the busiest ever for our nation's air travelers. Many are hopeful that this recovery in air traffic will lift revenues in the aviation trust fund, outweighing the effects of lower fares charged by the airlines. One study predicts a steady increase in trust fund revenues starting this year and revenues rising to over $17 billion in the next decade.

At issue today is the health of the Airport and Airway Trust Fund and what measures, if any, should be taken to alter its revenue sources. Some have suggested switching to a "user fee" system adopted in other countries, in which fees are assessed per flight segment based on a number of factors. These factors include the weight of the aircraft, the distance of the flight segment, and the usage of airports with a heavier volume of air traffic. Other aviation interests would like to remain with the status quo, in which a series of fees and taxes are collected at the point of sale by the government. One thing is certain: there is wide disagreement within the aviation industry as to just how robust the trust fund is, and whether or not we should change the way the trust fund collects revenues.

NATA is in a position unique to all others testifying before you today, as our association represents businesses that contribute to the trust fund through both excise and fuel taxes. Carriers that provide non-scheduled air charter service under Part 135 regulations are classified as commercial air carriers and pay the same excise taxes and segment fees as scheduled airlines. NATA also represents hundreds of fixed-base operators (FBO) throughout the country, who provide services such as maintenance, fuel, and hangar space to general aviation aircraft. With our membership encompassing a broad range of the aviation industry, the association feels that funding for the trust fund should remain with the structure we currently have in place, a combined system of excise taxes and fuel taxes. While there are certainly a number of questions that need to be answered before Congress contemplates any change in the current funding structure for the aviation trust fund, it is critical that Congress is aware that overall a system of user fees could add greater confusion and inefficiency to the air transportation system, cause a bureaucratic nightmare for both government and industry, jeopardize safety at small airports, and ultimately result in less revenue than in the current system.

Federal Aviation Administration Funding

President Bush's Fiscal Year 2006 budget paints a bleak picture for the Federal Aviation Administration (FAA). The President's budget proposes a $55 million cut in the FAA's operations budget, a $2.45 billion cut in the FAA's Facilities and Equipment account, and a $500 million cut in the Airport Improvement Program. Trust fund revenues are expected to reach their lowest levels in almost seven years. Also, the Administration is looking to the trust fund as the sole fundraiser for the FAA. This year, almost 85 percent of the FAA's operations budget will come from trust fund revenues, a dangerous trend that further dilutes the trust fund's original aim of providing a fund for airport and infrastructure funding.

Although these numbers present a sobering view of the state of the aviation industry in the eyes of the government, the FAA presently continues to receive every cent it has asked for from Congress. In the current year, Fiscal Year 2005, the FAA has received 100 percent of its budget request from Congress, yet the agency has still implemented plans to slow down a number of vital programs, including certification of important safety programs. NATA members across the country have received letters from their local Flight Standards District Office stating that any new safety and security programs in need of certification will have to wait due to funding constraints. Attached to my testimony are letters from FAA officials country-wide informing NATA members that they will have to wait on certification of their innovative safety initiatives until more funding is presented. Important procedures that will improve the safety of air transportation are left in limbo, despite the fact that the FAA is supposedly operating with all the resources it needs for this year.

Perhaps the biggest impediment to reforming the trust fund is the FAA's great difficulty in accurately predicting its costs and needs. If the FAA cannot properly assess its costs for any given year, why should we embark on the reform of a system that we're not sure is even in trouble yet?

The On-Demand Air Charter Industry

NATA is the sole representative of on-demand air charter operators in the United States. Despite perceptions that commercial air service strictly encompasses traditional hub and spoke airlines, on-demand charter operators are absolutely considered commercial air carriers. Operating under Part 135 regulations, air charter services charge the same 7.5 percent excise tax and $3 segment fee that the scheduled airlines collect. Comprising over 2,800 operators and generating close to $5 billion per year in revenues, the charter industry is one of the fastest growing segments in the aviation industry. Many Americans are realizing the value of eschewing the traditional air travel system and utilizing charters, which allow passengers to take off and land at many additional airports, including more convenient airports in small communities, without the hassle of connecting flights and long lines.

Unfortunately, in the context of this discussion, it is nearly impossible to determine precisely how much on-demand charter carriers contribute to the trust fund. With the industry comprising primarily small businesses operating with just a small number of aircraft and a small group of employees, obtaining data from all charter businesses is quite difficult.

False Statements Regarding General Aviation's Trust Fund Contribution

In the debate over the future of the Airport and Airway Trust Fund, representatives from the airline industry have repeatedly made the claim that general aviation does not pay its fair share into the trust fund. Nothing could be further from the truth. I have already stated the role of the on-demand air charter industry, which pays the same taxes and fees as the airlines. In fact, one could argue that air charter passengers actually contribute more to the trust fund than they would if they flew on a scheduled air carrier, as charter fees are almost always larger than airline fares. Other general aviation aircraft contribute to the system in the form of a fuel tax on general aviation jet fuel and gasoline. I will describe the benefits of the fuel tax later.

Those who claim that general aviation does not contribute to the trust fund base that claim on general aviation's utilization of the Air Traffic Control (ATC) system. The truth is that the ATC system in the United States was designed for and currently caters to scheduled airlines. The traditional hub and spoke model used by most airlines was firmly in the minds of those who first designed the air traffic control system, and very little has changed over the last 40 years. Despite contributing to the trust fund in the same manner as airlines, Part 135 operators get no special treatment when it comes to air traffic control restrictions. In heavily congested air traffic areas, charter and general aviation traffic are the first to see their flight plans curtailed, while the FAA does very little to reduce airline service into a particular airport. When the FAA issues Special Traffic Management Programs (STMPs) to prepare for special events that bring in unusual volumes of air traffic, airlines are allowed to keep their normal schedule of operations while non-scheduled aircraft are required to follow a number of burdensome restrictions.

Inequitable restrictions are also applied as a result of security measures as the FAA fulfills its role in monitoring the airspace. Whenever a Temporary Flight Restriction (TFR) is put in

place, usually when the President is traveling or special events such as last summer's political conventions are taking place, non-scheduled aircraft are prohibited from entering the airspace of the TFR. That policy usually affects an entire airport and, therefore, grounds all general aviation traffic sitting at that airport, while airlines are able to fly right through the airspace and use the airport as if there were no restrictions at all. Such government enforced policies that clearly favor scheduled airlines while punishing general aviation add no strength to the argument that general aviation receives equal treatment and, therefore, should have to pay into the system in the same manner as the airlines.

The Role of the General Aviation Fuel Tax in the Trust Fund

General aviation aircraft, with the exception of on-demand charter operators, contribute to the trust through a fuel tax, which has been in place since 1970. Currently, the fuel tax is set at 21.9 cents per gallon for jet fuel and 19.8 cents per gallon for general aviation gasoline. The tax is collected at the point of sale, when a pilot pays for fuel at an FBO or other fueling station. The fuel tax has proven to be the most cost effective and efficient manner of collecting revenues from general aviation aircraft. With a direct payment of the tax into the trust fund, there is no need for an unwieldy bureaucracy to collect the tax. If Congress is prepared to call the 18-cents-per-gallon gasoline tax a user fee for the Highway Trust Fund, than certainly you can see the logic in a fuel tax for general aviation aircraft. The fuel tax for general aviation aircraft is the fairest way to allow users of small aircraft to pay into the airport and airway trust fund.

The fuel tax has the potential to bring in more revenues to the trust fund than user fees in the years to come. According to FAA forecast statistics, over the next decade, the number of general aviation hours flown in a given year is expected to increase by roughly 5 million hours, while fuel consumption is expected to increase by almost a *billion* gallons. This explosion in fuel consumption will likely be related to the coming debut of very light jets (VLJs) on the market, which will fly much faster than current general aviation aircraft but also consume more fuel. The revenues generated from this increase in fuel consumption should surely give a boost to trust fund revenues.

Problems Associated With User Fees

Imposing a user fee system in the United States similar to those used by Canada or European countries will cause significant problems for the general aviation industry. Although supporters of a user fee system point to successful implementation in other countries, this Committee already knows the extreme difficulty of comparing foreign air transportation systems with that of the United States. General aviation traffic in the United States dwarfs other countries in comparison. According to National Transportation Safety Board statistics, in 2003 the United States logged 25.8 million hours of general aviation flight time, compared with just 1.67 million in Canada.

Perhaps the greatest argument against user fees is the bureaucratic and administrative disaster that looms if such a system is implemented. If the United States were to adopt a system similar to Canada's, flights would be billed after the trip has been completed. Aircraft

operators would receive these bills sometimes weeks and months after the flight, and busier operators can generate multiple bills per day and hundreds in a particular week. The general aviation industry is not equipped to handle this enormous accounting burden. While airlines will be able to check schedules and use the overall size of their operation to more efficiently audit their fight activity, small businesses, including air charter operators, will not have the resources to perform such audits. They will have to rely on the good faith of the FAA that they are being accurately assessed for their activity.

The unique nature of the on-demand industry also presents a problem for user fees in that charter operators sometimes have little advance notice as to a client's destination and when they are departing. Charter businesses could generate enough bills from the FAA to require hiring additional employees to review and match each bill to the operator's records to ensure that the company is being properly billed. Ninety percent of all Part 135 operators have less than 25 employees and generate less than $5 million in revenue every year. These operators could not possibly justify having dedicated staff to review bills submitted to them by the FAA or a similar corporate entity.

Although user fees would wreak havoc on the general aviation industry, the burden imposed on the FAA could be even worse. In an agency that is already claiming significant budget problems, establishing an office responsible for assessing every flight segment in the entire air transportation system would prove to be a bureaucratic nightmare. Even if the FAA delegated the responsibility to a corporate entity, the oversight needed by the agency would cut into any forecasted gains in revenues under this new system and drive up the FAA's already "tight" operating budget. As an example, we've been hearing about the FAA's air traffic control modernization plans since the early 1980s and look where we are today. Do any of you on this panel honestly have faith in the FAA's ability to accurately and efficiently keep track of and properly assess every single flight segment in the United States? I doubt many of you do.

Another advantage the current system holds over a proposed user fee system is the protection aviation businesses receive from the Internal Revenue Service when it comes to collecting taxes. In many cases, air charter operators bill their clients after the trip is completed. If the client refuses to pay a bill or attempts to pay a lesser amount, the client is still liable to the IRS for the excise taxes and segment fees generated by the flight. The IRS holds the customer of the air service responsible for paying those fees and does not punish the aviation business for their clients' unscrupulous behavior. In a user fee system, these businesses would need to be offered the same protection in the liability of fees currently offered by the IRS. Without a guarantee that the business will not be held accountable, most charter operators would find it difficult to support any user fee system.

In addition to the economic issues I have described that could arise with a user fee-based system, safety concerns present another significant problem. Presumably, a user fee system will charge an aircraft based on the level of air traffic control services it receives over the course of a particular flight. In a country with thousands of small airports, many lacking any air traffic control services, user fees would discourage numerous operators from using safer air traffic control systems and cause them to decide to use airports with limited or no air

traffic control service to avoid the hefty fees that come with use of those services. Imagine a situation where aircraft owners, in an attempt to cut costs, begin to use smaller, rural airports with no control tower rather than more technically advanced airports. Smaller airports will be unable to handle the increased volume of traffic in a safe and secure manner, and the overall safety of the air transportation system would be compromised.

Conclusion

You have heard a number of arguments today regarding the current and future financial condition of the trust fund and what we should or should not do in the future to ensure a healthy trust fund balance. As a representative of segments of the aviation industry that contribute via both excise and fuel taxes, NATA has seen the effects of each method of payment. While any business would prefer to lower its overall tax burden, the aviation businesses represented by NATA are eager to contribute to the trust fund to make certain that our nation's aviation infrastructure is maintained and expanded in the decades to come.

The current system is the most fair and efficient way to proceed in collecting trust fund revenues. While scheduled airlines contribute the majority of revenues into the fund, they receive more than preferential treatment in the air traffic control system. On-demand charter and general aviation operators contribute to the trust fund in a manner that reflects their usage of the air traffic control system. Air charter operators, which are commercial air carriers just like scheduled airlines, contribute through the same system of ticket taxes and segment fees as scheduled airlines. Other general aviation aircraft have been contributing to the fund through fuel taxes for over 35 years. Fuel taxes leave no open questions regarding the collection of taxes for a particular flight. Every gallon is taxed equally, no matter where the aircraft is flying.

All of us here today appreciate the FAA's foresight in looking to the future of the aviation industry and into methods of improving our nation's infrastructure in a rapidly changing environment. NATA applauds Administrator Blakey for opening a dialogue on this important issue and listening to the voices of every facet of the industry on this subject. We feel that the system of funding currently in place is the best way to ensure a fair and guaranteed funding stream into the Airport and Airway trust fund. As the FAA and Congress continue to evaluate the changing needs of America's aviation industry, NATA is eager to work hand in hand with them in improving the system.

Thank you for the opportunity to testify, and I will be happy to answer your questions.

U.S. Department of Transportation
Federal Aviation Administration

Baltimore Flight Standards District Office

890 Airport Park Road, Ste.101
Glen Burnie, Maryland 21061
410-787-0040, Fax: 410-787-8708

March 14, 2005

David Russell
President
American Flight Group, Inc..
1974 B & A Blvd
Annapolis, MD 21401

Dear Mr. Russell:

Processing Delay

The Baltimore FSDO has received your application package for RVSM approval for aircraft N770MC, N581AS, and N244LJ.

Due to budget limitations and staffing shortages, our FSDO has had to implement a plan for managing new Certification requests.

We will keep your material, enter it into our backlog, and start on it as soon as an opening is available. Due to our previously stated limitations, it may take as long as 90 days for us to complete the process.

Please accept our apology for not being able to give you faster service. We appreciate your understanding and patience in this matter.

Sincerely,

John P. Barry
Assistant Manager

U.S. Department of Transportation
Federal Aviation Administration

Southwest Region
Arkansas, Louisiana
New Mexico, Oklahoma,
Texas

Fort Worth, Texas 76193-0000

MAR 0 4 2005

Mr. Richard McFadden
Associated Air Center
P.O. Box 540728
Dallas, TX 75234

Dear Mr. McFadden:

We have reviewed your application package dated January 31, 2005, for a Supplemental Type Certificate (STC) for installation of an executive interior in an Airbus A319 aircraft.

Please be advised that given our current limited resources and reduced staffing, as well as our financial outlook for this and the next fiscal year, it compels us to evaluate the resources required to support your program in light of other FAA Aircraft Certification Service priorities. This evaluation will affect the timelines for your program. It would be unfair to accept your project without informing you that we may not be able to support the timelines you desire. As we have done in the past, we plan to sequence the flow of projects to stay within our available resources. The difference this year is that the resources are severely limited so we need to determine the costs and overall FAA priorities before we commit to individual projects.

We anticipate being able to tell you when we can commence work on your project within the next 3 months. The application package is acceptable, and does provide us with the initial information we need to begin processing your project, so you do not need to resubmit what you have already provided. Please use tracking number 2005021401 for reference on any correspondence. If you have any questions, please contact me at 817-222-5190.

Sincerely,

S. Frances Cox
Manager, Special Certification Office
Aircraft Certification Service

cc:
ASW-100
AIR-1
AIR-2

U.S. Department
of Transportation
**Federal Aviation
Administration**

Small Airplane Directorate
Wichita Aircraft Certification Office
1801 Airport Road, Room 100
Wichita, Kansas 67209

February 28, 2005

Ms. Dawn Wingfield
Certification Manager
Sabreliner Corporation
7733 Forsyth Blvd.
Suite 1500
St. Louis, MO 63105-1821

Subject: Type Design Change

Dear Ms. Wingfield:

We acknowledge receipt of your application dated February 17, 2005, 05SC-005, for a Supplemental Type Certificate (STC) for Sabreliner Model NA-265-40.

Please be advised that our current limited resources and reduced staffing, as well as our financial outlook for this and the next fiscal year, compel us to evaluate the resources required to support your program in light of other FAA Aircraft Certification Service priorities. This evaluation will affect the timelines for your program. It would be unfair to accept your project without informing you that we may not be able to support the timelines you desire. As we have done in the past, we plan to sequence the flow of projects to stay within our available resources. The difference this year is that the resources are severely limited so we need to determine the costs and overall FAA priorities before we commit to individual projects.

We anticipate being able to provide you a response about when we will be able to commence work on your project within the next 3 months. In the meantime, we have assigned project number TD4263WI-T to your application. Please use this number for reference when corresponding with this office about your application. If you have any questions, please contact me at (316) 946-4106, or Mr. Grant Youngdahl, your project manager for this application, at (316) 946-4171.

Sincerely,

for Lorial M. Condotta
Margaret Kline
Manager
Wichita Aircraft Certification Office

Copy to: Directorate Manager
AIR-1/2

United States Government Accountability Office

GAO

Testimony

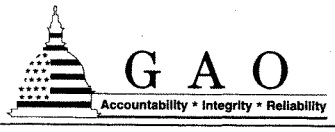
Before the Subcommittee on Aviation, Committee on Transportation and Infrastructure, House of Representatives

For Release on Delivery
Expected at 10:00 a.m. EDT
Wednesday, May 4, 2005

AIRPORT AND AIRWAY TRUST FUND

Preliminary Observations on Past, Present, and Future

Statement of Gerald L. Dillingham, Ph.D.
Director, Physical Infrastructure Issues



GAO-05-657T

May 4, 2005

GAO
Accountability·Integrity·Reliability

Highlights

Highlights of GAO-05-657T, a report to Subcommittee on Aviation, House Committee on Transportation and Infrastructure

AIRPORT AND AIRWAY TRUST FUND

Preliminary Observations on Past, Present, and Future

Why GAO Did This Study

The Airport and Airway Trust Fund (Trust Fund) was established in 1970 to help fund the development of a nationwide airport and airway system and to fund investments in air traffic control facilities. It provides all of the funding for FAA's accounts such as the Airport Improvement Program (AIP), which provides grants for construction and safety projects at airports, the Facilities and Equipment (F&E), which funds technological improvements to the air traffic control system, and the Research, Engineering, and Development (RE&D). In addition, the Trust Fund provides some funding for FAA's operations account. To fund these accounts, the Trust Fund relies on a number of taxes for revenue, including passenger ticket, fuel, and cargo taxes that are paid by passengers and airlines. Since 1970, revenues have generally exceeded expenditures —resulting in a surplus or an uncommitted balance. In 2004, the Trust Fund's year end uncommitted balance was about $2 billion.

A number of structural changes in the aviation industry and external events have affected revenues flowing into and out of the Fund and have caused some aviation stakeholders to speculate about the Fund's financial condition. The various taxes that accrue to the Trust Fund are scheduled to expire in 2007. GAO was asked to provide information and analysis about the financial outlook of the Trust Fund.

www.gao.gov/cgi-bin/getrpt?GAO-05-657T.

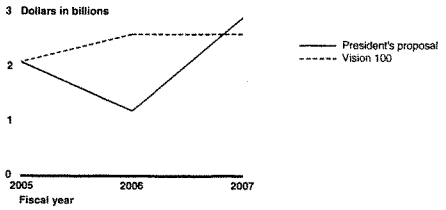
To view the full product, including the scope and methodology, click on the link above. For more information, contact Gerald Dillingham at (202) 512-2834 or dillinghamg@gao.gov.

What GAO Found

With the exception of its first four years, the Trust Fund has ended each year with an uncommitted balance; however, the amount of the uncommitted balance has fluctuated and is currently trending downward. In 1991 and 1999, the Trust Fund's uncommitted balance totaled over $7 billion—its highest level. However, in several years, the Trust Fund's balance experienced dramatic decreases resulting in a lower uncommitted balance, in part, because of lapses in the taxes that accrue to the Fund or reductions in demand for air travel. The Trust Fund's uncommitted balance decreased from $7.3 billion in 2001 to $4.8 billion in 2002 and has continued to decrease by about $1 billion each year since. This declining uncommitted balance has been caused by a number of underlying factors, such as reductions in the demand for air travel.

Over the next 3 years, the Trust Fund is projected to have sufficient revenue to fund authorized spending and end each year with an uncommitted balance under the current law, referred to as Vision 100, and the President's 2006 budget proposal, as shown below. However, this financial outlook depends on the realization of FAA's forecasted commercial passenger traffic levels and airfares. If revenues are 5 percent lower than projected, as they were in 2001, the Trust Fund's uncommitted balance would be $1.5 billion or lower under both Vision 100 and the President's budget proposal in 2006 and 2007. If the revenues were 10 percent lower than projected, as they were in 2004, the uncommitted balance would reach zero in 2006 under the President's proposal and in 2007 under Vision 100. FAA officials told GAO that if the uncommitted balance reached zero, FAA would still fund air traffic control services but would have to suspend some AIP and F&E activities.

Trust Fund's Projected Year End Uncommitted Balance Under Vision 100 and President's 2006 Budget Proposal



Source: FAA.

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss the financial condition of the Airport and Airway Trust Fund (Trust Fund). The Trust Fund was established by the Airport and Airway Revenue Act of 1970 (P.L. 91-258) to help fund the development of a nationwide airport and airway system and to fund investments in air traffic control facilities. It provides all or some of the funding for FAA's accounts which include the

- Airport Improvement Program (AIP), that provides grants for construction and safety projects at airports,
- Facilities and Equipment (F&E) account that funds technological improvements to the air traffic control system,
- the Research, Engineering, and Development (RE&D) account, and
- Operations account.

To fund these accounts, the Trust Fund relies on a number of taxes for revenue, including passenger ticket, fuel, and cargo taxes, that are paid by passengers and airlines. In fiscal year 2004, the Trust Fund received $9.7 billion in revenue and had expenditures of $10.4 billion.[1] Although Trust Fund expenditures exceeded revenues in 2004, since its creation in 1970, revenues have generally exceeded expenditures —resulting in a surplus or an uncommitted balance.[2] At the end of 2004, the Trust Fund's uncommitted balance was about $2.4 billion, a decrease of about 67 percent since 2001.[3]

A number of structural changes in the aviation industry and external events have affected revenues flowing into and out of the Trust Fund and have caused some aviation stakeholders to speculate about the Fund's financial condition. For example, some aviation stakeholders believe that there is a reason to be concerned about the financial condition of the Trust

[1]For purposes of this report, we are using the expenditure amount rather than the appropriated amount. The expenditure amount includes the amount of funding spent on AIP, F&E, RE&D, and operations and does not include commitments.

[2]The Trust Fund's uncommitted balance represents money against which there is no outstanding budget commitment or authority to spend.

[3] All dollar amounts in this testimony are in nominal dollars.

Fund because revenues have not recently kept pace with expenditures. In contrast, other aviation stakeholders state that the Trust Fund is healthy because revenues are expected to continue increasing. The various taxes that accrue to the Trust Fund are scheduled to expire in 2007.

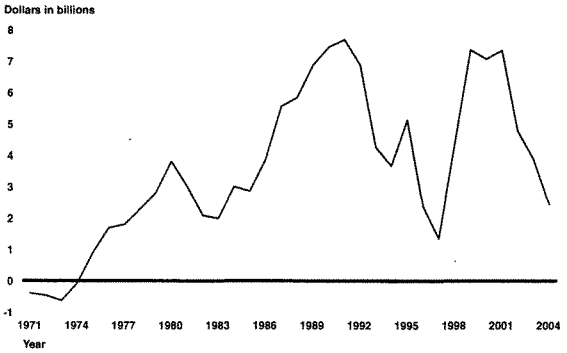
My statement today is based on our ongoing work on the Trust Fund and discusses our preliminary observations on the past, present, and future financial outlook of the Trust Fund. We plan to issue a final report to this Subcommittee later this year.

Historically, Trust Fund Has Generally Had an Uncommitted Balance but Recently the Balance Has Started to Trend Downward

As shown in figure 1, with the exception of its first four years, the Trust Fund has ended each year with an uncommitted balance; however, the amount of the uncommitted balance has fluctuated and is currently trending downward. In 1991 and 1999, the Trust Fund's uncommitted balance totaled over $7 billion, which represented its highest amount.[4] However, in several years, the Trust Fund's experienced dramatic decreases resulting in a lower uncommitted balance. For example, in 1982, the end of year uncommitted balance was $2.1 billion, and in 1997 it was $1.4 billion because of a lapse in the taxes that accrue to the Trust Fund. The Trust Fund's uncommitted balance also decreased from $7.3 billion in 2001 to $4.8 billion in 2002 and has continued to decrease by about $1 billion each year since. There are a number of reasons for this downward trend, including changes in the amount of revenue flowing into and out of the Trust Fund.

[4] Because of price level increases that reduced the value of a dollar over time, in terms of purchasing power, the Trust Fund was larger in 1991 than in 1999.

Figure 1: Trust Fund's Uncommitted Balance Has Recently Started to Trend Downward

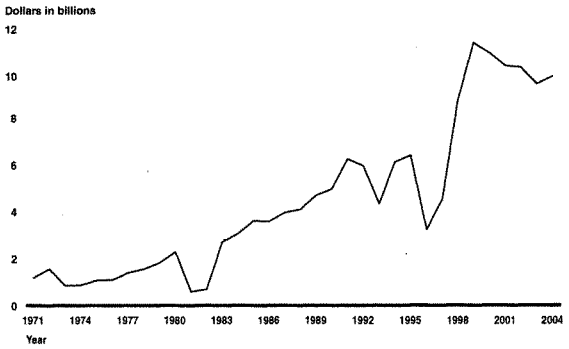


Source: Congressional Budget Office and FAA budgets.

Revenues Have Generally Increased With Some Fluctuations

The amount of revenues flowing into the Trust Fund has fluctuated from year to year but has generally trended upward, as shown in figure 2. The Trust Fund relies on a number of taxes for revenue, including passenger ticket, fuel, and cargo taxes that are paid by passengers and airlines. During 1981 and 1982 the amount of revenues including interest flowing into the Trust Fund averaged $629 million which was the lowest amount in its history because of a lapse in the collection of aviation taxes. In contrast, in 1999, revenue flowing into the Trust Fund totaled $11.1 billion, which was the largest amount in its history.

Figure 2: Trust Fund Revenues Have Fluctuated but Generally Increased



Source: Congressional Budget Office and FAA budgets.

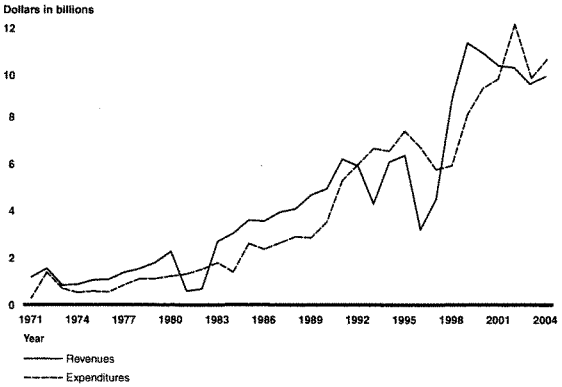
However, after revenues peaked in 1999, the amount of revenue flowing into the Trust Fund started to trend downward, totaling $9.7 billion in 2004. A number of factors may have contributed to this decrease. For example, within the airline industry, the growth of the Internet as a means to sell and distribute tickets, the growth of the low cost airlines, and fare reductions by legacy carriers all transformed the industry and led to lower average fares. These lower fares may have resulted in lower ticket taxes and less revenue into the Trust Fund.[5] In addition, a series of largely unforeseen events, including the September 11 terrorist attacks, war in Iraq and associated security concerns, the Severe Acute Respiratory Syndrome (SARS), global recessions, and a steep decline in business travel seriously reduced the demand for air travel resulting in a sharp decrease in airline industry revenue.

[5]Increased traffic from these lower fares may have offset some of the decline in tax revenue.

Trust Fund Expenditures Have Also Increased and Exceeded Revenue in Some Years

The amount of funds flowing out of the Trust Fund also has generally increased since the Fund's inception and has also exceeded revenues in some years. For example, as shown in figure 3, from 2002 through 2004, expenditures exceeded revenues by an average of about $938 million, or about 9 percent.

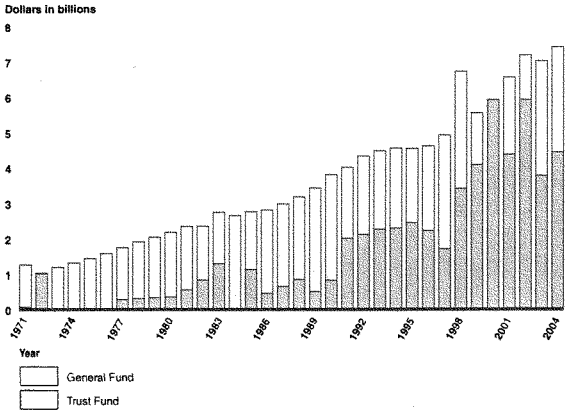
Figure 3: Expenditures Exceeded Revenues in Some Years



Source: Congressional Budget Office and FAA budgets.

As mentioned earlier, the Trust Fund provides all the funding for AIP, F&E, and RE&D and provides some funding for operations. Trust Fund expenditures have grown because of increases in both spending for these accounts and in the amount of FAA operations funded by the Trust Fund. For example, the amount of funding provided for AIP increased from about $1.5 billion in 1998 to $3.5 billion in 2005. In addition, as shown in figure 4, since its inception the Trust Fund has funded some portion of FAA's operations. In 1972 and 2000, the Trust Fund funded 100 percent of the cost of FAA operations. In 2004, the Trust Fund funded 60 percent and it is expected to fund 63 percent in 2005.

Figure 4: FAA Operations Cost Funded By Trust Fund and General Fund

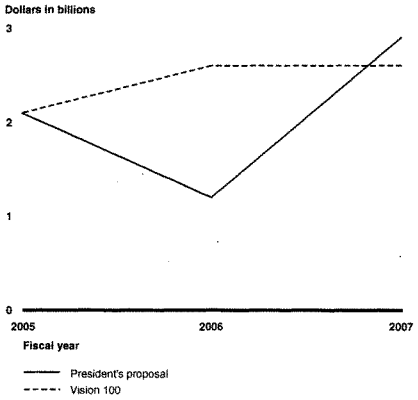


Source: FAA

Projected Trust Fund's Uncommitted Balance Is Positive but Depends on Realization of Forecasted Passenger Traffic Levels and Airfares

Over the next 3 years, the Trust Fund is projected to have sufficient revenue to fund authorized spending and end each year with an uncommitted balance under Vision 100 and the President's 2006 budget proposal. However, this financial outlook depends on the realization of FAA's forecasted commercial passenger traffic levels and airfares. As shown in figure 5, under the current law—the Century of Aviation Reauthorization Act (Vision 100)—the Trust Fund's year-end uncommitted balance is projected to be about $2.6 billion in 2006. Under the President's proposal, it is projected to be slightly over $1 billion in 2006.

Figure 5: Trust Fund's Projected Uncommitted Balances Under Vision 100 and President's Budget Proposal



Source: FAA.

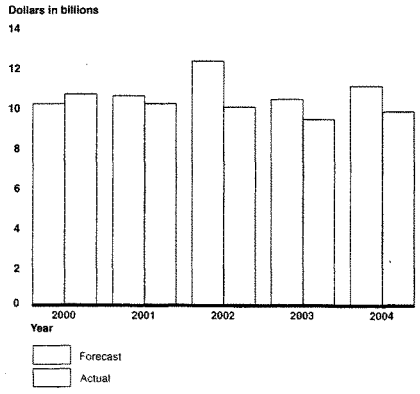
The primary reason that the Trust Fund's uncommitted balance would be higher under Vision 100 is that it uses the formula created in the Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR-21) to determine how much funding for FAA Operations should come from the Trust Fund, and the President's proposal does not. Under AIR-21, the formula sets the amount of Trust Fund revenue that will be authorized for FAA Operations in a given year equal to projected Trust Fund revenues (as specified in the President's budget) minus the authorizations for AIP, F&E, and RE&D in that year. Thus, under Vision 100, the Trust Fund is projected to support almost $15 billion, or 63 percent of FAA Operations from 2005 through 2007. In contrast, the President's proposal specifies a set amount of Trust Fund revenue to be used for FAA Operations. Therefore, if Congress enacts the President's proposal, the Trust Fund would provide $17.7 billion for FAA Operations from 2005 through 2007, or about 74 percent of its total estimated costs for Operations.

In contrast to 2006, in 2007, the Trust Fund's uncommitted balance would be about $300 million higher under the President's budget proposal than

under Vision 100. According to FAA officials, this is primarily because of reduced spending for AIP and F&E under the President's budget proposal.

Although the Trust Fund is projected to have a positive uncommitted balance from 2005 to 2007 under each of the expenditure proposals, this projection depends to a significant extent on achieving forecasted commercial passenger traffic levels and airfares that affect the amount of revenues flowing into the Trust Fund. We recognize that it is very difficult to anticipate future events that may significantly affect the demand for air travel and our analysis shows FAA's projected revenue forecast exceeds the actual amount of revenue received for four of the last five years as shown in figure 6. According to FAA officials, the major reasons why projected revenues were lower than actual revenues is because forecasted airline yields[6] were higher than the actual yields and aviation activity was below anticipated levels for the last several years.

Figure 6: Comparison of Forecasted Revenue with Actual Revenue Received



Source FAA budgets.

[6]Yields are commonly measured in cents per revenue passenger mile—with revenue passenger miles being the number of miles revenue passengers are transported.

Given the difference between the forecasted revenue and actual amount of revenue received, we conducted sensitivity analyses to estimate what would happen to the Trust Fund's uncommitted balance if passenger traffic or yields fall below the levels that FAA projected in November 2004. For example, table 1 shows the projected Trust Fund balances under Vision 100 and the President's proposal and the impact if revenues are 5 percent or 10 percent less than currently projected. If revenues are 5 percent lower than projected, as they were in 2001, the Trust Fund's uncommitted balance would be $1.5 billion or lower under both Vision 100 and the President's budget proposal in 2006 and 2007. However, if the revenues are 10 percent lower than projected, as they were in 2004, the uncommitted balance would reach zero in 2006 under the President's proposal and in 2007 under Vision 100.

Table 1: Sensitivity Analysis of the Trust Fund's Uncommitted Balance to Revenue Shortfalls

Dollars in millions				
Revenue scenario	**Fiscal year uncommitted balance**			
Proposal		**2005**	**2006**	**2007**
Baseline projections as of November 2004	Vision 100	$2,103	$2,571	$2,615
	President's budget	2,103	1,195	2,937
If revenues are 5 percent less than projected	Vision 100	1,577	1,459	855
	President's budget	1,577	83	1,176
If revenues are 10 percent less than projected	Vision 100	1,051	346	0
	President's budget	1,051	0	0

Source: GAO analysis of FAA data.

A scenario in which the Trust Fund reaches zero is cause for concern. According to FAA officials, the elimination or reduction of the Trust Fund's uncommitted balance could also pose budgetary challenges. For example, if the Trust Fund's uncommitted balance reached zero in 2006 it might require FAA to make significant spending cuts to aviation programs currently supported by the Trust Fund unless additional funding were authorized and appropriated from the General Fund. According to FAA officials, they would continue to fund air traffic control services because it is considered an emergency function that involves the safety of human life. However, to fund air traffic control services, FAA officials said it would

have to suspend activities for AIP, F&E, and RE&D accounts including some F&E contracts.

Regarding the long-term financial outlook of the Trust Fund, we believe that it is difficult to project beyond 2007 because the Trust Fund expires in 2007 and it is unknown if the current tax schedule will change. In addition, as mentioned earlier, forecasting aviation activity is difficult in part because of the complexities and uncertainties associated with anticipating future events that may affect the demand for air travel. Projecting the long-term financial outlook of the Trust Fund also requires some consideration of the planned spending of the programs that it finances.

According to FAA officials, over the next 4 years, there may be an $8.2 billion dollar gap between costs and revenues, which reflects a $5 billion shortfall for operations and $3.2 billion shortfall for capital development. If this projected gap is realized, our past work suggests that the cost saving initiatives that FAA has identified will not be sufficient to close this gap.[7] Consequently, additional reductions will be needed. For example, to meet air traffic controller staffing needs FAA could consider making greater use of the Air Traffic Collegiate Training Initiative Program which could save millions of dollars annually. In addition, FAA could save millions of dollars by eliminating redundant ground based navigational aids.

Concluding Observations

Deciding what changes may need to be made to the Trust Fund to help ensure a safe, efficient, and adequately funded national airspace system will require some tough choices by Congress and FAA. One of the critical questions that will need to be addressed is not only the amount of the Trust Fund's uncommitted balance but also whether the government has the fiscal capacity to fund current and future Trust Fund obligations while concurrently addressing the needs of other competing programs for scarce resources.

FAA and Congress will also have to find a way to better align FAA's costs with revenue and to better address both the cost and revenue sides of the ledger. In terms of cost savings, our past work suggests that the cost saving initiatives that FAA has identified will not be sufficient to close its

[7] U.S. Government Accountability Office, *National Airspace System: Progress and Ongoing Challenges for the Air Traffic Organization*, GAO-05-485T (Washington, D.C.: April 14, 2005).

projected 4-year cumulative $8.2 billion shortfall. On the revenue side, this decision-making will include the consideration of a number of alternatives that have been proposed by various aviation stakeholders— ranging from increasing the current taxes that accrue to the Trust Fund to adopting user fees that would be more cost related— and the trade-offs associated with each. We plan to review these alternatives as part of our ongoing review of alternative approaches for funding FAA that we are doing at the request of this Subcommittee.

This concludes my statement. I would be pleased to answer any questions that you or other members of the Subcommittee may have.

Contacts and Acknowledgments

For further information on this testimony, please contact Dr. Gerald Dillingham at (202) 512-2834 or by email at dillinghamg@gao.gov. Individuals making key contributions to this testimony include, Jay Cherlow, Tammy Conquest, Colin Fallon, David Hooper, Maren McAvoy, and Nicolas Zitelli.

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The Airport and Airway Trust Fund: Preliminary Observations on Past, Present, and Future

Gerald Dillingham, Ph.D.
Director, Civil Aviation Issues
U.S. Government Accountability Office

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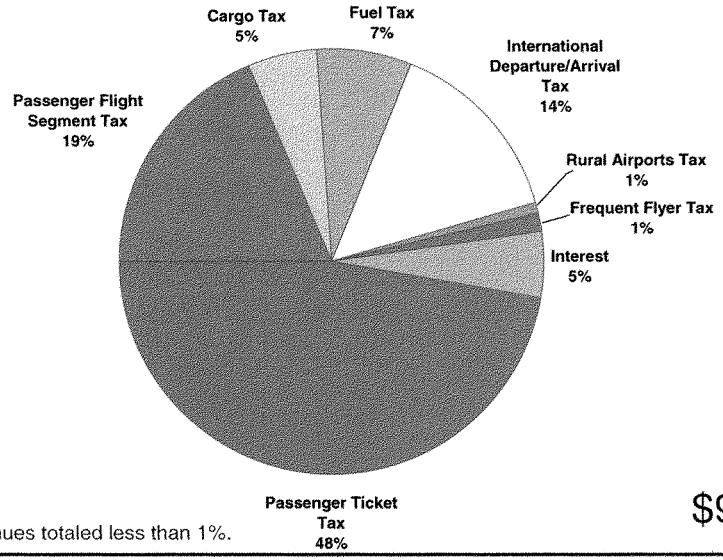
Sources of Trust Fund Revenue, FY04



$9.7 billion

Note: Other revenues totaled less than 1%.

Source: Congressional Budget Office and FAA Budgets.

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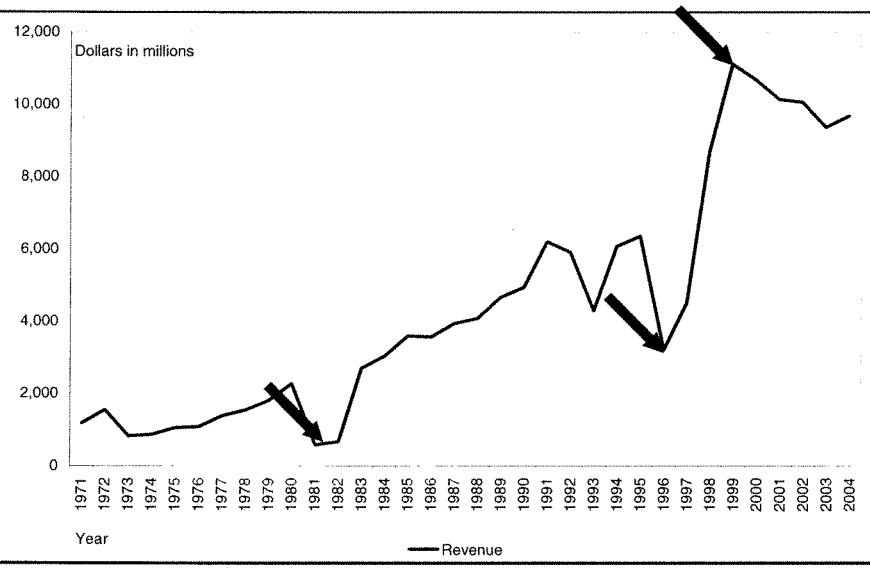
Trust Fund Revenues Have Fluctuated but Generally Increased



Source: Congressional Budget Office and FAA Budgets.

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Factors Contributing to Decline

- September 11, 2001 terrorist attack
- SARS outbreak
- Iraq war
- Growth in low-cost carriers
- Fare reductions by legacy carriers

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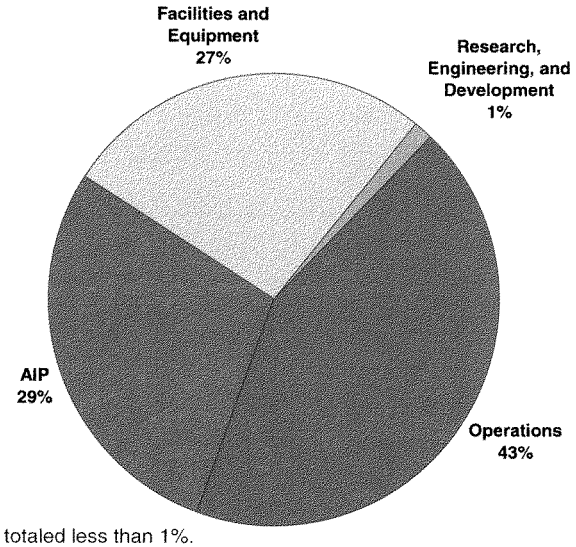
Allocation of Trust Fund Expenditures, FY04



$10.4 billion

Note: Other expenditures totaled less than 1%.

Source: Congressional Budget Office and FAA Budgets.

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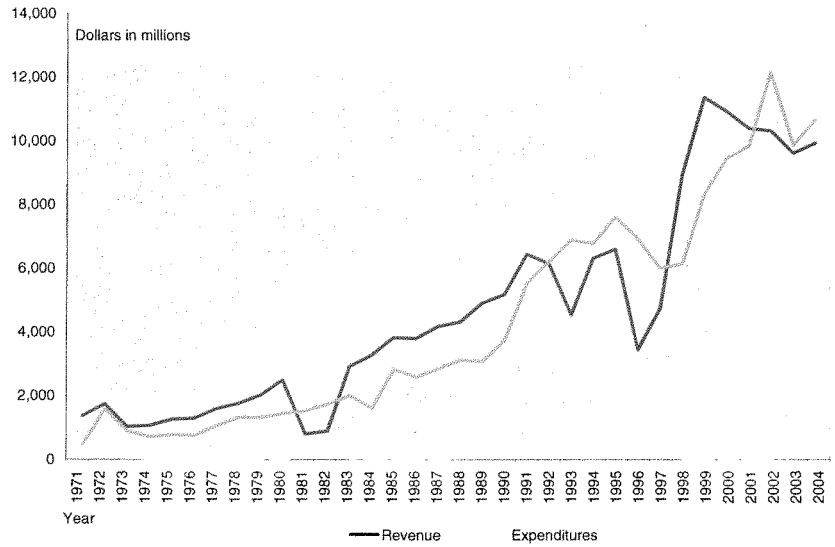
Expenditures Exceeded Revenues in Some Years



Source: Congressional Budget Office and FAA Budgets.

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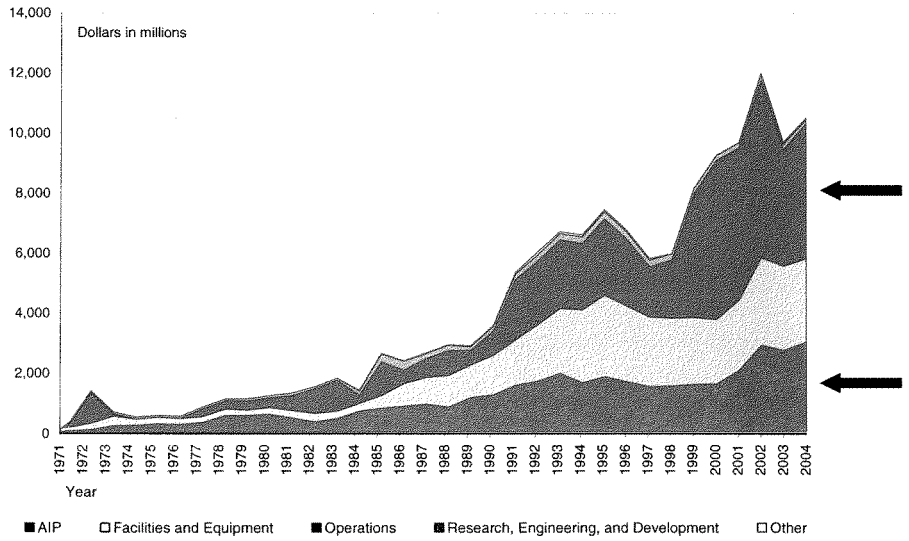
Trust Fund Expenditures Have Generally Increased in the Major Accounts



Source: Congressional Budget Office and FAA Budgets.

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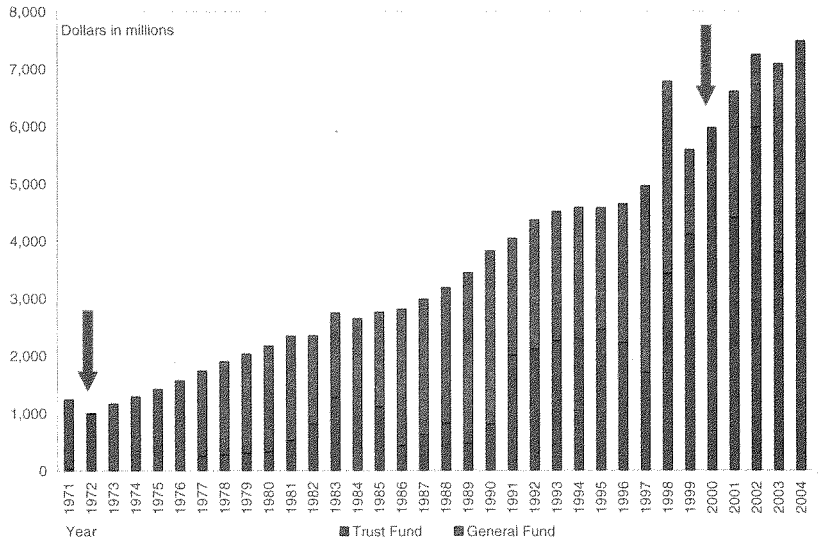
FAA Operations Cost Funded by Trust Fund and General Fund



Source: FAA.

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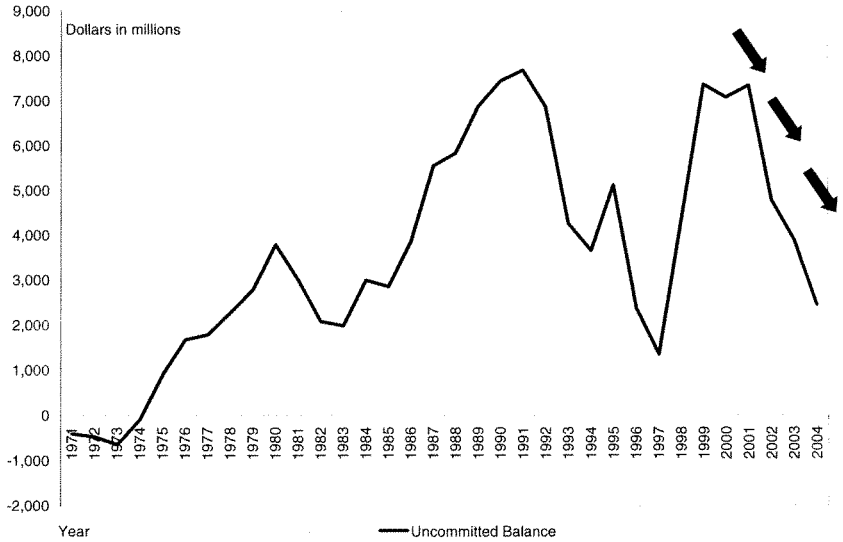
Trust Fund's Uncommitted Balance Has Recently Started to Trend Downward



Source: Congressional Budget Office and FAA Budgets.

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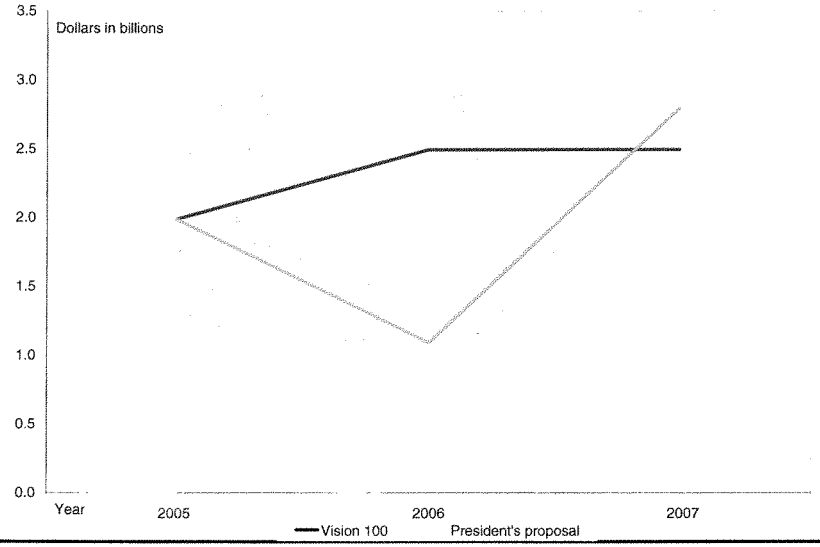
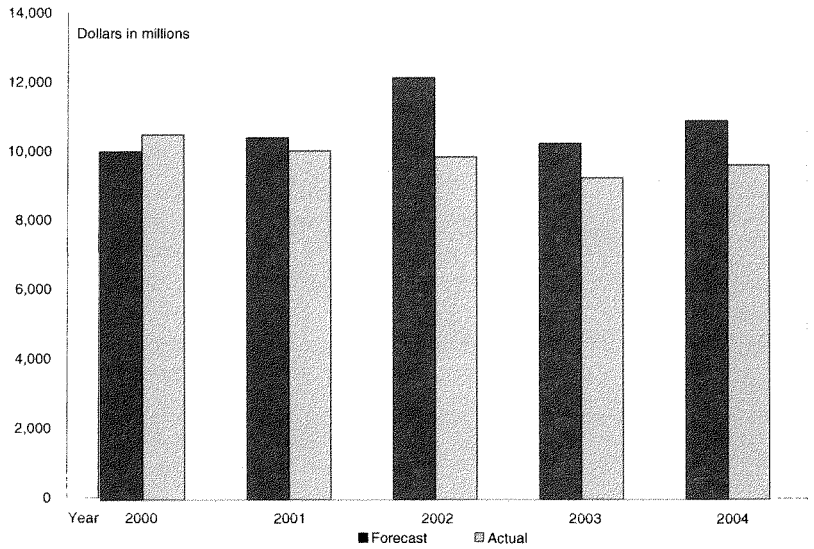
Trust Fund's Projected Uncommitted Balances



Source: FAA.

Comparison of Forecasted Revenue with Actual Revenue Received



Source: GAO Analysis and FAA.

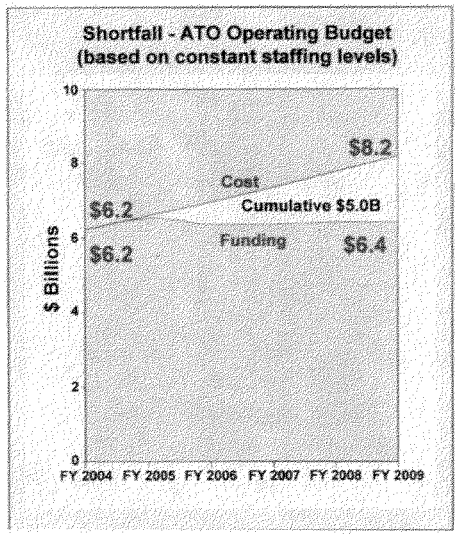
Sensitivity Analysis of the Trust Fund's Uncommitted Balance to Revenue Shortfalls

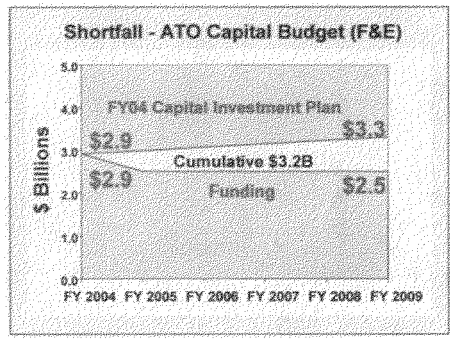
- If revenues are 5 percent less than projected, the Trust Fund would have a small but positive uncommitted balance under both Vision 100 and the President's 2006 budget proposal.

- If revenues are 10 percent less than projected, the Trust Fund's uncommitted balance would reach zero in 2006 under the President's proposal and in 2007 under Vision 100.

Source: FAA and GAO Analysis

Reasons for Concern: ATO's Projected Shortfalls





Source: FAA

Next Steps for Addressing Revenue and Cost

- Strategic business plan needed
- Several financing options being discussed
- Cost control initiatives

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U.S. House of Representatives
Committee on Transportation and Infrastructure
Washington, DC 20515

Don Young
Chairman

Lloyd A. Jones, Chief of Staff
Elizabeth Megginson, Chief Counsel

James L. Oberstar
Ranking Democratic Member

David Heymsfeld, Democratic Chief of Staff

June 3, 2005

Dr. Gerald Dillingham
Director, Physical Infrastructure Issues
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Dr. Dillingham:

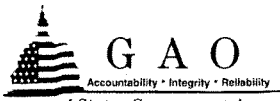
On May 4, 2005, the Subcommittee on Aviation held a hearing on the "Financial Condition of the Aviation Trust Fund: Are Reforms Needed?

Attached is a question from Rep. James L. Oberstar to answer for the record. I would appreciate receiving your written response to this question within 30 days so that it may be made a part of the hearing record.

Sincerely,

Jerry F. Costello
Ranking Democratic Member
Subcommittee on Aviation

JFC:pk
Attachment



United States Government Accountability Office
Washington, DC 20548

June 16, 2005

The Honorable James L. Oberstar
U.S. House of Representatives
Committee on Transportation and Infrastructure
2365 Rayburn HOB
Washington, DC 20515-2308

Re: Question for the Record from the Subcommittee on Aviation, May 4, 2005 Hearing on "Financial Condition of the Aviation Trust Fund: Are Reforms Needed?"

Dear Congressman Oberstar:

In your June 3, 2005 letter, you asked me a question regarding my prepared remarks from the above-titled hearing. In those remarks, I stated that if the Aviation and Airway Trust Fund's (Trust Fund) uncommitted balance reached zero in 2006, it might require the Federal Aviation Administration (FAA) to make significant spending cuts to aviation programs currently supported by the Trust Fund unless additional funding was authorized and appropriated from the General Fund. More specifically, we stated that FAA would continue to fund air traffic control services, but that it would have to suspend activities for Airport Improvement Program (AIP), Facilities and Equipment (F&E), and Research, Engineering, and Development (RE&D) accounts including some F&E contracts. You asked for a technical explanation including the operative authority (statutes, etc.) that would produce the results we described.

According to FAA officials, if the Trust Fund's uncommitted balance were to reach zero, the agency would have to suspend activities for the AIP, F&E, and RE&D programs to continue to fund operations, unless Congress authorized funding from the General Fund. For example, FAA might have to delay or terminate some multimillion dollar F&E contracts, such as the National Aerospace System Implementation Services contract, which provides engineering support for the implementation of programs such as the Standard Terminal Automation Replacement System. FAA officials also stated that while their contracts have clauses that limit liability, it is their experience that any remaining obligated funds for contracts in a given fiscal year that have not been expended would be used to offset contract termination costs.

FAA's decision to suspend activities for the AIP, F&E, and RE&D programs and use the funds appropriated for these suspended capital programs to first fund Operations would not be based on any statutory requirement, but on FAA's determination that

the continued function of the air traffic control system must take priority over its other accounts. Air traffic control is considered an emergency function that involves the safety of human life. Also, FAA would have to obtain specific transfer authority from Congress to move money from the AIP, F&E and RE&D accounts to the operations account to fund the air traffic control system.

If the Trust Fund's uncommitted balance reaches zero, FAA would be generally prohibited from further spending due to the requirements of the Anti-Deficiency Act, 31 USC 1341, which prohibits an agency from obligating or expending funds in excess or in advance of appropriations. Another section of the Anti-Deficiency Act, 31 USC 1342, prohibits an agency from accepting voluntary services, such as in cases where an agency's appropriations has lapsed or been obligated or expended. However, there is an exception to this general prohibition on the acceptance of voluntary services by federal government agencies in 31 USC 1342 "for emergencies involving the safety of human life or the protection of property." FAA officials consider the air traffic control function to come under this exception.

Sincerely yours,

Gerald L. Dillingham, Ph.D.
Director, Civil Aviation Issues
Enclosure

cc: Representative Jerry F. Costello
Jim Coon, Staff Director
David Hemymsfeld, Staff Director
Stacie Soumebniotis, Minority Counsel
Pamela Keller, Democratic Staff Assistant

Committee on Transportation and Infrastructure

Aviation Subcommittee

Financial Condition of the Aviation Trust Fund:

Are Reforms Needed?

May 4, 2005

Testimony of Edward P. Faberman, Executive Director

1776 K Street, N.W., Ninth Floor
Washington, D.C. 20006
202-719-7420
epfaberman@acaa1.com

COMMITTEE ON TRANSPORTATION & INFRASTRUCTURE

AVIATION SUBCOMMITTEE

Financial Condition of the Aviation Trust Fund:

Are Reforms Needed?

Testimony of Edward P. Faberman, Executive Director

Air Carrier Association of America

May 4, 2005

Mr. Chairman, I ask that my full comments be made part of the record for this hearing. Thank you.

Chairman Mica, Ranking Member Costello, Members of the Committee – It is a pleasure to appear before you today to discuss an issue that is critical to the continued economic growth of communities throughout our country and to the expansion of airline service by low-fare carriers – that issue is the future funding of the Airport and Airway Trust Fund. Mr. Chairman, we believe that changes must be made to the funding of the FAA. In making those changes, however, it is critical for the expansion of competition and for job and economic growth in communities throughout this country that we not discourage passengers from traveling.

Our goals for this review are to:

- Ensure plentiful, high quality, low cost air transportation;
- Minimize congestion-related delays both in air and on ground;
- Minimize transaction costs;
- Provide good long-term incentives for aviation financing, including the FAA budget and infrastructure improvements.
- Ensure all communities are fairly treated.

Taxes and fees added to fares that are stimulating traffic can increase those fares by 20% to 40%. Data clearly shows that large numbers of travelers will forego certain trips if fares – including taxes and fees – are increased by even 10%.

One of the comments we have heard is that due to lower fares, the government is not receiving the same quantity of fees and taxes as collected in the past. Let me present to you a different perspective on this point. With lower fares, business and leisure travelers have returned to the skies. They are taking multiple trips and traveling with others. Load factors are at record levels.

We are better off with a passenger taking five business trips at $200 per roundtrip than if that passenger took one business trip at a $750 fare. Lower fares also allow family members to accompany travelers and allow businesses to send multiple people to a meeting instead of one person. Therefore, a greater quantity of fees and taxes are paid as a result of the travel stimulated by the lower fares.

A larger problem impacting trust fund investment is the number of seats available on aircraft. For example, a 120 seat aircraft contributes significantly more to the federal government and airports through excise taxes, PFCs, and landing fees than a 50-seat jet.

Despite the horrific events of 9/11, new security procedures, and unexpected costs, we have witnessed a rebirth of the U.S. airline industry.

As a direct result of the expansion of competition, particularly from low-fare carriers, into new domestic markets, Americans are returning to the skies. As Secretary Mineta stated at the FAA Commercial Aviation Forecast Conference in Washington, D.C. on March 17, 2004:

> ...the combination of shifting demand for air travel, and the emergence of more low-fare airlines, has set the stage for major change in the airline industry... demand is still off, demand for low-fare service is strong and growing stronger. We think that the changes that are underway now are the kind of market-based, cost competition that the architects of deregulation thought would happen 25 years ago. Consumers are driving these changes – and that, ultimately, is a very healthy development.
>
> Demand continues to grow. We are forecasting that more passengers will fly this year than did in the previous peak year of 2000. And we are looking ahead to more than one billion passengers by 2015.
>
> But the domestic business travelers who would pay any price for a ticket – formerly the bread and butter for the major network carriers – have not returned, and probably never will.
>
> Deregulation has delivered a dynamic industry, where consumers are driving change. Airline customers have more options, at lower fares, based on more timely information, than ever before – and our economy is better off as a result.

Additionally, in a speech on March 10, 2004 at the Commercial Club of Chicago, Secretary Mineta stated, "A healthy transportation sector is essential to President Bush's efforts to keep America on track for a more prosperous future...Transportation has never been more important to America's economic future than it is right now."

American travelers in communities from throughout the country are searching for more affordable travel alternatives. The ability of low-fare carriers to offer price and service alternatives has increased demand for their services.

As I noted earlier, a major problem that is adding to congestion and delays is the increased use of regional jets. The DOT Inspector General's Report, "Airline Industry Metrics, Trends on Demand and Capacity" dated January 8, 2004, states that:

> Delays at some Airports are increasing...some airports are beginning to experience increases over the past years...Chicago O'Hare reported 44, 230 arrival delays during the first 11 months of 2003...In some months, however, the number of delays was significantly greater. According to FAA, the problems at O'Hare stem from aggressive scheduling by the airlines as American has shifted many of its prior St. Louis connections to Chicago and United has responded competitively by scheduling head-to-head operations. FAA also attributes United's use of regional jets to match American's schedule with further reductions in airport capacity, as regional jets require greater separation times between operations than do larger jets.
>
> Another significant development involves the phenomenal growth in RJ flights. Scheduled flights involving RJs increased 140 percent (from 88,474 to 212,126) between December 2000 and December 2003. Flights involving other aircraft types experienced far less growth or sharp declines, including piston (+10 percent), large jets (-19 percent), and turboprop (-41 percent). Overall, the portion of scheduled flights involving RJs has grown from 10 percent to 25 percent between December 2000 and December 2003.
>
> RJs are also assuming a larger share of the total number of scheduled flights at the 31 largest airports. Those airports with the highest percentages of RJ flights as of December 2003 are: Cincinnati (72 percent), Dulles (44 percent), Chicago O'Hare (41 percent), Houston (39 percent), Newark (38 percent), St. Louis (36 percent), Dallas-Ft. Worth (35 percent), Salt Lake City (34 percent), LaGuardia (30 percent), and Reagan National (29 percent).

In the FAA NPRM on "Delay Reduction and Operating Limitations at Chicago O'Hare" (Docket No. FAA-2005-20704), the FAA addresses why O'Hare delays are worse than ever:

> But by 2003, the two air carriers operating hubs at O'Hare, American Airlines ("American") and United Airlines ("United") had added a large number of operations and retimed other flights, resulting in congestion during peak hours of the day. From April 2000 through November 2003, American increased its scheduled operations at O'Hare between the hours of 12:00 p.m. and 7:59 p.m. by nearly 10.5 percent. Over the same period, United increased its scheduled operations at O'Hare by over 41 percent.
>
> Overall, American and United added over 600 regional jet operations per day. The result was a decrease in seat capacity by each carrier at O'Hare of more than 5.5 percent from April 2000 to November 2003. In November 2003, more than 40 percent of American's and United's O'Hare flights were operated with regional jets, many to large and medium hubs. The significant increases in scheduled

operations during this time period resulted in excessive delays and congestion at O'Hare.

By November 2003, O'Hare had the worst on-time performance of any major airport. O'Hare arrivals were on time only 57 percent of the time, well below the FAA goal of 82 percent. Departures were little better. They were on time only 67 percent of the time, well below the average of 85 percent at other airports. These delays averaged about an hour in duration. Published schedules for February 2004 indicated that the problem would be exacerbated by the addition of even more flights.

The DOT Inspector General's report, "Airline Industry Metrics, Trends on Demand and Capacity," dated January 8, 2004, also demonstrated that the increased use of regional jets by American and United is creating the ATC problems at O'Hare. The report states that FAA officials have acknowledged that the reason delays are increasing in the Chicago area is due to the "growth in regional jets."

To this end, it is essential that all operators of aircraft pay their fair share of the costs they create for the FAA. At a time when we see projections of dramatic increases in "personal" jet usage, those operators, particularly when they are going to a congested airport and traveling through congested airspace, must contribute the same fees paid by carriers.[1] We believe it is critical for the FAA to establish standard costs for operating through airspace and at airports, and to determine whether those costs differ based upon the size of the aircraft involved.

Although low-fare high efficiency carriers have had reasonable financial results in the past few years, many of their costs continue to increase. These increasing costs include fuel, security, airport fees, and air traffic system congestion. Since you are aware of the impact that rising fuel costs have had on the industry, let me address other costs:

Security – In addition to the security fees charged on each ticket, carriers are routinely asked to pay for construction to add new security equipment at airports, (charges that TSA was supposed to pay for), additional security staffing, and costs for delayed or cancelled flights because of security problems.

Airports – At many airports, carriers have been hit with increased landing fees and facility costs to reimburse airports for their additional expenses, lower passenger numbers, and for security construction costs.

Air Traffic Control System – Due to the significant increase in smaller aircraft and general aviation aircraft operating in the system, ATC delays have increased in several parts of the country including southern Florida, Chicago, and

[1] USA Today, April 25, 2005, "On-Demand Airlines Could Alter Travel to Midsize Cities." There have been multiple stories about small jets (5-7 seats) being utilized to fly people to markets nationwide. The small jet operators include Dayjet and Pogo – that may operate hundreds of new aircraft.

> New York. Smaller carriers have been hit particularly hard by delays and congestion, which also adds to their costs.

Fortunately, while many travelers and communities benefit from increased low-fare travel opportunities, true competition remains a dream in some markets because of increased costs of operation and barriers that continue to block entry and expansion. Costs of operation and congestion may limit expansion or entry for low-fare carriers.

The need to promote entry of new entrants into all markets was recognized as an essential part of deregulation. As Alfred Kahn noted:

> The key to lower prices and improved efficiency is competition, and the key to competition is competitors... A downward zone, without entry, would not reliably produce lower prices, since the threat of entry – not charitable motives – is the only sure incentive for carriers to reduce their prices. And upward fare freedom – again, absent freedom of entry – poses an immediate threat of exploitation of consumers in all those markets where regulation under the present Act has failed to create competition. The proposed bill would make it easier for carriers to enter new markets in three important ways, and for that reason, more than any other, we support it.
>
> Testimony of Alfred Kahn, Hearings before the Subcommittee on Aviation, House Committee on Public Works and Transportation on HR 11145 (Airline Regulatory and Reform Hearing), March 6, 1978

The Deregulation Act emphasized the importance of entry into all airports. Competition and new entry are the backbones of airline deregulation. In order for deregulation to continue and expand, we must adhere to the following:

> (10) Avoiding unreasonable industry concentration, excessive market domination, monopoly powers..., and
>
> (13) Encouraging entry into air transportation markets by new and existing air carriers and the continued strengthening of small air carriers to ensure a more effective and competitive airline industry. (49 U.S.C. §40101)

If a new entrant is advised that it will have to now pay higher fees to travel to and enter an airport that is already congested, because incumbent operators have flooded that airport with operations, it may avoid that airport. To maintain an open and competitive market place, prospective entrants must be provided with access on reasonable terms which will result in more competition, which in turn, results in lower average fares and better service for air travelers.

To allow entry and to ensure the future health and growth of the ATC system, we recommend that the following points be considered as part of any review of FAA and ATC funding issues:

1. Due to the enormous impact that commercial air service has on the nation's economy, the general fund must continue to help fund the ATC system;
2. All system operators' contributions must be based upon the costs they impose on the system. Therefore, whether a flight involves two passengers or 150, it should contribute the same amount in terms of fees and taxes;[2] and
3. A carrier or any operator that conducts a large number of operations at an airport and increases operations that create further delays and ATC problems, should be charged an additional amount to conduct those operations.

At the same time, the FAA needs to identify the specific actions that create or increase costs. Which costs should be applied to each operation and do costs vary with aircraft size or time of day of a specific operation? Do certain airports create higher costs to the system?

We need to move forward with this review but care must be taken not to block competitive opportunities or to establish yet another barrier to entry. Costs and airport facility problems have blocked new entrants from establishing competitive operations at numerous airports across the country.

Times are changing and to ensure that all travelers are able to seek competitive low fare service, all parties involved including the government, airports, and carriers must consider requirements to expand the joys of airline deregulation.

I thank you for again focusing on issues that impact true airline competition. We believe that all communities should be able to enjoy low-fare service. We look forward to working with you to make that a reality while at the same time expanding the nation's air traffic control system. The founders of deregulation would not have it any other way. I would be delighted to take any questions.

---

[2] Efficient prices are in principle equivalent to marginal cost. Marginal costs of airports and for the ACT system are not materially affected by (1) aircraft weight, (2) number of passengers, or (3) level of ticket prices.

Yet these three factors largely determine current price signals to airline users.

An efficient congestion minimizing pricing system will consider the real marginal costs imposed on the system, especially the time dimension.

For runways: Time = Distance and Speed
For ATC generally: Time = Distance and Speed
Altitude
Technology
Geography

Opening Statement of Congressman Tim Holden
House Aviation Subcommittee hearing on
The Financial Condition of the Aviation Trust Fund
May 4, 2005

Mr. Chairman, Ranking Member Costello--thank you for holding this important hearing to assess the financial condition of the Aviation Trust Fund and discuss possible alternative methods of funding the future needs of the aviation system.

I share the FAA's concern with the declining uncommitted cash balance of the Trust Fund and appreciate the opportunity to begin a dialogue on these critical issues well in advance of the next FAA reauthorization in 2007.

I look forward to hearing our witness's comments and suggestions on what changes they see as appropriate for the future financial needs of the FAA.

Personally, I am very keen on the idea of granting some sort of bonding or borrowing authority to give the FAA the ability to provide the necessary investment in a timely manner to modernize the air traffic control system without requiring the users to pay the entire investment cost up front.

Currently, the FAA has to purchase from current budget amounts, meaning that they have to spread out purchases over ten years or so, giving an incremental approach to modernization that is out of date before it is finished.

By using the power to bond, the FAA would be able to design projects and purchase state of the art equipment, and then repay over a number of years. If that were the case, we might be able to eliminate some of the finger-pointing as to why the agency is slow to respond to facility needs.

For instance, the Harrisburg International Airport in my Congressional District recently went through an FAA Part 150 noise study to see what noise impact it has on the local populace. Some of the recommendations that made sense were to modify some of the procedures of aircraft taking off -- in particular, to keep some a little higher before making turns and making some minimum altitudes a few hundred feet higher. Every one of the suggested changes was really very minimal, and would not have negatively affected any airline, or aircraft.

The FAA however, said it would not approve any changes without going through an environmental assessment, and since there isn't any money to do one, it will be several years before one can be done, thereby putting off the completion of this study for several years.

I would be interested to hear from Administrator Blakey and any other witness today how a situation like the one we have at Harrisburg could be better addressed with the ability to borrow or bond.

Clearly we need to plan now for financial stability in the future with regard to our aviation system. Changes will need to be made and some savings will need to be achieved. However Mr. Chairman, one proposal I disagree with the FAA on is its proposal to close 42 of its air traffic control towers from midnight to 5 AM. When applying the simplest of cost benefit analysis to this proposal, I do not feel the potential savings it would achieve are anywhere near enough to merit the risks to safety closing the towers would present. Administrator Blakey, I have some questions regarding this proposal that I would like to ask you when we get to the appropriate time in the hearing.

Thank you Mr. Chairman, I yield back.

Statement of Ruth E. Marlin
Executive Vice President
National Air Traffic Controllers Association
Before the Committee on Transportation and Infrastructure
Subcommittee on Aviation
United States House of Representatives
May 4, 2005

Financial Condition of the Aviation Trust Fund

Good morning Chairman Mica, Congressman Costello, and members of the Subcommittee. I want to thank you for this opportunity to appear before the Subcommittee to discuss the financial condition of the Aviation Trust Fund.

I am Ruth Marlin, Executive Vice President of the National Air Traffic Controllers Association (NATCA), the exclusive representative of over 14,525 air traffic controllers serving the FAA, Department of Defense and private sector. In addition, NATCA represents approximately 1,200 FAA engineers, over 600 traffic management coordinators, agency operational support staff, regional personnel from FAA's logistics, budget, finance and computer specialist divisions, and agency occupational health specialists, nurses and medical program specialists.

NATCA's mission is to preserve, promote and improve the safety of air travel within the United States, serve as an advocate for air traffic controllers and other safety-related employees, and promote competence and pride within our profession. We are also proud of our efforts promoting technological advances, providing reliable and accurate information for our members, and serving as a credible source of information for this Committee, the traveling public, and the news media.

Over thirty years ago the Airport and Airway Trust Fund was established to ensure adequate capital investment in our nation's aviation infrastructure. Since its inception, the U.S. has used the Trust Fund to make capital improvements: investing in airports; air traffic control facilities and equipment; and research and development.

The structure Congress set up for the Trust Fund has provided consistent growth with few exceptions. Those exceptions, or fluctuations in revenue, are largely attributable to external factors, such as economic or policy decisions. The structure also permitted surpluses to build up over time allowing the Trust Fund to provide stable funding through those brief periods of revenue decline. Through the Trust Fund, investment in our nation's aviation infrastructure has resulted in the most accessible, affordable and efficient aviation system in the world.

It is an accepted fact that while the Trust Fund revenue experienced a temporary period of decline from 2000 through 2003, revenues rebounded in 2004. However, that has not stopped opponents of the current Trust Fund structure from attempting to shift the debate from revenues to trust fund balances. All indicators point to continued and future growth in Trust Fund revenues. However, if congressional appropriators follow the Administration's budget request and reduce the general fund contribution, the result will be a greater allocation from the Trust Fund and yes, balances may decline as a result. This is not a crisis; it is a policy decision.

We welcome the public discussion of this critical policy decision, and we were dismayed when the Federal Aviation Administration announced on Monday their intention to dissolve the Trust Fund at the end of the current budget allocation period in 2007. We believe a robust discussion of this topic is in order before rushing to conclusions that may not serve our nation's safety, security and economic best interests.

Revenues are closely tied to the volume of air travel. The FAA predicts a record 718 million passengers will travel this year and that number is expected to grow to one billion

passengers by 2015. Under the current structure of the Trust Fund, each domestic passenger pays both a segment fee and a 7.5% excise tax on every ticket purchased while each international passenger pays an international departure fee. Even if average airfares dropped to $100, the increase in the number of travelers alone would account for an additional $3 billion a year in Trust Fund revenue.

Proponents of change are quick to mention yield, seat miles, users fees or a nebulous metric such as a "unit of production" as possible revenue indicators. NATCA believes that a critical safety function like air traffic control is better served by not attempting to obfuscate the funding discussion with corporate market choices. While more aircraft flying with more empty seats may cause yield to go down, we are not talking about legroom here. Our discussion is about funding our national aviation infrastructure and operating air traffic control, an essential safety function. There are plenty of forums in which we can debate whether or not U.S. airlines are making sound business decisions, and I think the US bankruptcy court is doing that as we speak.

Ironically, the last time the Trust Fund was due for reauthorization the debate focused on addressing the increasing Trust Fund surpluses. For decades the Trust Fund surplus has been a source of controversy, leading to legislation increasing expenditures. Now, a few short years later, some government and industry officials suggest that reducing the surplus is no longer desirable. Additionally, it is being used as evidence for their allegation that the fund is now structurally deficient.

NATCA maintains that the Aviation Trust Fund surpluses have provided a valuable source of stability, allowing our national aviation investment to continue through periods of brief decline so that program cuts are not made today that curb our nation's long term economic growth. In recent years, there have been dramatic fluctuations in the use of the Trust Fund to fund normal operations costs. An examination of the way the Trust Fund has been used since its last reauthorization illustrates the flexibility that our current structure provides the U.S. Congress.

	1997	1998	1999	2000	2001	2002	2003	2004
Operations	4,953	5,253	5,586	5,958	6,926	7,077	7,023	7,479
Trust Fund	1,700	1,902	4,112	5,958	4,405	5,973	3,775	4,469
General Fund	3,253	3,351	1,474	(-11)	2,521	1,104	3,248	3,010
Aviation User Fees	(12)	28			30	28		
AIP (Trust)	1,460	1,640	2,322	2,799	2,597	3,173	3,378	3,647
F&E (Trust)	1,938	1,900	2,121	2,034	2,667	3,006	2,942	2,863
R&D (Trust)	208	199	150	156	189	245	147	118

Source: Office of Management and Budget - Department of Transportation (Federal Aviation Administration- Federal Funds

Our nation's aviation system benefits the entire country, not just the people who fly. Civil aviation accounts for 9 percent of our gross domestic product – that's over 900 billion dollars and over 11 million jobs. Americans enjoy the best and safest aviation system in the world because of the structure built many years ago whose foundation rests on resources drawn both from the aviation taxes and the general public. Reducing the contribution made by the public through general revenue could degrade the system, reduce efficiency and safety and restrict economic growth. These costs will be borne by every citizen not just the aviation industry.

NATCA is not asserting that more money is needed to fund the FAA or the operations budget. We understand the strains on the federal budget. However, while we do not think that large increases from the general fund are needed, we also do not believe that major cuts are appropriate. For four of the eight years since the Trust Fund taxes were reauthorized, the general fund contribution for FAA operations exceeded $3 billion. However, the structure of our funding mechanism allows Congress to adjust the balance between the Trust Fund and general revenue as circumstances dictate. Recognizing the significant national interest in maintaining and operating our air traffic control system, NATCA believes that Congress has acted properly in making these determinations.

Oddly enough, the opponents of the current funding system cite eliminating the role of Congress in the financial decision making process as a reason for abandoning our current

structure. NATCA disagrees. We are talking about the safety of hundreds of millions of passengers every year, about an infrastructure that is a powerful economic engine, about the mobility of the citizens of our country, and NATCA believes the people we elect to represent us have a role to play in those decisions.

Another common argument from trust fund opponents is the need to replace many of our air traffic control facilities. Yes, there are many facilities in need of repair or replacement, and many programs are funded and ongoing. In just the last five years, despite the tremendous financial pressures on the system, the FAA has replaced more than 30 Air Traffic Control Towers and Terminal Radar Approach Control facilities. That is an average of one every two months. Yet, to hear the rhetoric today, you would think we hadn't opened a new facility in 30 years, that replacing air traffic control facilities is an insurmountable task. Nothing could be further from the truth. In fact, I would argue that in the United States we have more experience opening new air traffic control facilities in the last five years than most providers have in their entire history.

For some reason, we are not hearing this part of the story. Two years ago we all heard about the new state of the art facility down the road when the Potomac Consolidated TRACON opened to replace the aging radar rooms in Baltimore, Dulles, National and Richmond. Since then we have also opened the Northern California TRACON, replacing older facilities in Oakland, Monterey, Sacramento and Stockton as well as one in New England replacing TRACON's in Manchester and Boston. New towers or TRACONS may not be making news in D.C. but they certainly have in Orlando, Atlanta, Philadelphia, Manchester, Addison, Savanna, Roanoke, Richmond, Columbus, Newark, Miami, Sioux City, Birmingham, St. Louis and Portland to name just a few.

Do we have facilities that are in need of replacement? Yes, absolutely. Many of our Centers are over forty years old. And much like this grand old Rayburn House Office Building, first constructed in 1965 and in which this hearing unfolds, our older air traffic control facilities are chock full of new computers, new equipment and new technology to

allow the workforce to do their jobs more safely and efficiently. The taxpayers and the American public get real value out of our older buildings, and those facilities will continue to function at high levels until it is their turn on the replacement waterfall.

In closing, NATCA believes we should not underestimate the strength of the current FAA funding system and we should not tamper with it lightly. The Trust Fund is a stable and strong source of revenue. We should keep it that way by rejecting radical changes based on a manufactured "crisis."

Understanding Air Traffic Control Financing

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April 2005

Understanding Air Traffic Control Financing
Ruth Marlin, National Air Traffic Controllers Association, AFL-CIO

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April 2005

About the Author

Ruth Marlin, the executive vice president of the National Air Traffic Controllers Association, has made her career one of firsts: In 2000, as the first woman in the organization's history elected to the position and subsequently, in 2003, when she became the first person ever reelected to the office.

In 1999, Marlin completed her first extensive research project on air traffic control issues. Her findings on controller retirement were later validated by the Federal Aviation Administration's workforce plan, as well as reprinted extensively, distributed internationally and translated into two languages.

Marlin holds a Bachelor of Arts in Labor Studies from the National Labor College and a Masters in Public Administration from the University of Baltimore. She is a member of the honor society Pi Alpha Alpha and a Doctoral Candidate in Public Administration. Her academic achievements led to her selection for Who's Who in American Universities and Colleges.

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Understanding Air Traffic Control Financing

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Executive Summary

The prime objective of air traffic services, as defined by the International Civil Aviation Organization (ICAO), "is to prevent collisions between aircraft, whether taxiing on the maneuvering area, taking off, landing, en route or in the holding pattern at the destination aerodrome."[1] ICAO also emphasizes that notwithstanding the organizational or financial structure of the service provision, air traffic control services remain a State obligation.

Over the last two decades, many air traffic control service providers have restructured from traditional government bureaucracies into organizational structures designed to be more responsive to the needs of system users. Restructuring may have been in response to financial pressures, air traffic congestion, a desire for regional harmonization, or part of broader government reforms. As a result there are a variety of different structures for both funding and corporate governance currently in place.

Developing an appropriate funding structure has presented new challenges for many States. The term privatization is broadly and imprecisely used to describe many different types of structures including commercialized entities that are wholly State owned. Within the air traffic community it is recognized that among major air traffic service providers, only the Canadian system is truly privatized while the United Kingdom system is part privatized. That is not to say that there is no common ground between the structural frameworks. Both privatization and commercialization address the funding mechanisms and corporate governance of the service provider.

In order to ensure that a national economy is able to maximize the benefits provided by a vigorous aviation industry, a reliable and robust air traffic control system is necessary as it is a critical component of the infrastructure. As air traffic control modernization in particular requires long term planning, a stable and predictable

[1] International Civil Aviation Organization, *The Convention on International Civil Aviation Annex 11-18. [online] http://www.icao.int/gil/goto_m.pl?icaonet/anx/info/annexes_booklet_en.pdf.*

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funding mechanism is required. Any funding mechanism constructed for the purpose of air traffic control service provision must meet the fundamental tests of providing both adequate and stable resources.

This study examines the major structures in place for the provision of air traffic services in North America, Europe, and Australia including their individual funding mechanisms. The purpose is to provide a fact-based framework for future policy discussion on the topic of air traffic control financing as States move to address weakness in the existing structures.

Introduction

The prime objective of air traffic services as defined by the International Civil Aviation Organization (ICAO) "is to prevent collisions between aircraft, whether taxiing on the maneuvering area, taking off, landing, en route or in the holding pattern at the destination aerodrome."[2] ICAO also emphasizes that notwithstanding the organizational or financial structure of the service provision, air traffic control services remain a State obligation.

The ICAO assembly is comprised of 188 contracting States established to promote civil aviation through cooperation and standardization:

> *One of ICAO's chief activities is standardization, the establishment of International Standards, Recommended Practices and Procedures covering the technical fields of aviation: licensing of personnel, rules of the air, aeronautical meteorology, aeronautical charts, units of measurement, operation of aircraft, nationality and registration marks, airworthiness, aeronautical telecommunications, air traffic services, search and rescue, aircraft accident investigation, aerodromes, aeronautical information services, aircraft noise and engine missions, security and the safe transport of dangerous goods. After a Standard is adopted it is put into effect by each ICAO Contracting State in its own territories. As aviation technology continues to develop rapidly, the Standards are kept under constant review and amended as necessary.*[3]

ICAO, as an agency of the United Nations, provides recommendations to contracting States, however, the actions of ICAO do not usurp the autonomy of sovereign States. Within the broad recommendations and guidance offered by ICAO, nations have adopted various organizational structures and funding mechanisms for air traffic service provision. This study will examine the dominant structures currently in

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2 Ibid.

3 ICAO's Aims: Standardization, http://www.icao.int/cgi/goto_m.pl?icao/en/aimstext.htm #Standardization.

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operation.

United States Model

An Overview

The United States air traffic control service is provided by the Federal Aviation Administration, a federal agency funded through the authorization and appropriations process used for most federal agencies. In addition to allocations from the general treasury, this process includes the distribution of revenue from the Airport and Airway Trust Fund.

The FAA is not a stagnant agency tied to a specific organizational structure. It has undergone substantial reforms to remain responsive to changing demands in civil and military aviation. The most recent reform takes advantage of several legislative steps in the process of creating a Performance Based Organization within the FAA. Recent reforms have gone beyond organizational structure and have included significant changes in both funding and corporate governance.

In the 1990's the FAA was granted sweeping exemptions from federal sector personnel and procurement regulations through HR2002, *The FY1996 Department of Transportation Appropriations Act*, and other legislation that provided minor amendments to its provisions. This Act provided the FAA with the flexibility to design personnel systems specific to the agency's mission without regard for most personnel regulations and systems in other parts of the Department of Transportation or the Federal Government. The Act sought to de-politicize the management of the FAA by establishing a five-year term appointment for the FAA administrator - extending beyond the elected term of the President making the appointment, and created the FAA Management Advisory Council (MAC) as well as the Air Traffic Services Subcommittee (ATSS). The MAC is an 18-member board that provides recommendations on aviation spending, policy, regulation and management, while the ATSS was constructed by Congress to oversee the Administrator's management of the air traffic control system.

In 2000, *The Wendell H. Ford Aviation Investment and Reform Act for the 21st*

Century sought to ensure that all revenue from aviation related taxes were expended for aviation purposes, rather than allowing large surpluses to continue to build up. These surpluses had traditionally been retained as an accounting device to reduce the appearance of the federal deficit. The Act also created the position of Chief Operating Officer (COO) within the FAA, for the air traffic control system. Later that year, the President issued Executive Order 13180 creating the Air Traffic Organization under the Chief Operating Officer. The COO is appointed to a five-year term to promote continuity of leadership, even though the term does not necessarily coincide with that of the Administrator.[4]

Rather than separate air traffic control services, the ATO consolidated the functions previously performed by separate lines of business within FAA. By consolidating Air Traffic Services, Research and Acquisitions, and Free Flight organizations, the ATO is able to manage both resources and decision-making related to air traffic service provision and investment. The COO reports directly to the FAA Administrator.

Financial Framework

The Airport and Airway Revenue Act of 1970 established the Airport and Airway Trust Fund for the purpose of funding the development of a nationwide airport and airway system and to fund investments in air traffic control facilities in order to meet the current and future projected growth in aviation.[5] The Act allowed aviation related excise taxes to be deposited in a trust fund for aviation activities. The primary taxes on passenger tickets and aviation gasoline were already in existence (since 1941 and 1932 respectively) and were previously deposited into the general fund. The Act created three new taxes on international tickets, air-freight waybills, and aircraft registration.

The Airport and Airway Trust Fund expired on October 9, 1980 at which point aviation-related excise taxes could no longer be deposited into the fund, leaving only the accumulated surplus from previous years. The Airport Improvement Act of 1982

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[4] Federal Aviation Administration, *FAA Air Traffic Organization*, November 17, 2003 (photocopied).

[5] General Accounting Office, Airport and Airway Trust Fund, (Washington, DC: GPO, 2003).

re-established the Airport and Airway Trust Fund and deposited $134 million from the general treasury into the Fund.

The *Omnibus Reconciliation Act of 1990* increased the passenger ticket tax from 8% to 10% of the fare, increased the cargo tax from 5% to 6.5%, and increased the rate for noncommercial jet fuel from 14 cents to 17.5 cents per gallon.[6]

In 1994 and 1996, a series of short-term reauthorizations extended the expenditure authority from the Trust Fund until January 1, 1997. The authority lapsed and was not reinstated until October 1, 1997, with the passage of the *Taxpayers Relief Act of 1997*. This Act reinstated the aviation excise taxes for ten years and set rates for taxes, gradually reducing the domestic passenger tax rate to 7.5% by 1999 while increasing flight segment fee to $3.00 by 2002 and indexing for inflation starting in 2003. The Act also set rates and indexing for the international passenger ticket tax, rural passenger taxes, special taxes for flight to Hawaii and Alaska, added other miscellaneous aviation related excise taxes and shifted the 4.3-cent per gallon aviation fuel from the general fund to the Trust Fund.

The *Wendell H. Ford Aviation Investment and Reform Act for the 21st Century*, enacted in April of 2000, substantially increased the annual funding for the Airport Improvement Program (AIP). It was intended to ensure that all revenue from aviation related taxes was spent on aviation programs through 2003. It allowed airports to raise passenger facility charges up to $4.50 and increased both the minimum and maximum annual funding available to large airports as well as raising the state apportionment and guaranteeing funding to general aviation airports for the first time.

The Trust Fund provides 100% of the funding for FAA airport grants (AIP), facilities and equipment, and research, engineering and development. Resources from the

Trust Fund, as well as an appropriation from the general fund, support FAA Operations. The percentage of Federal Aviation Administration operations that has

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[6] Eric Henry, *Excise Taxes and the Airport and Airway Trust Fund 1970-2002*, (Washington, DC: Statistics of Income Bulletin, 2003).

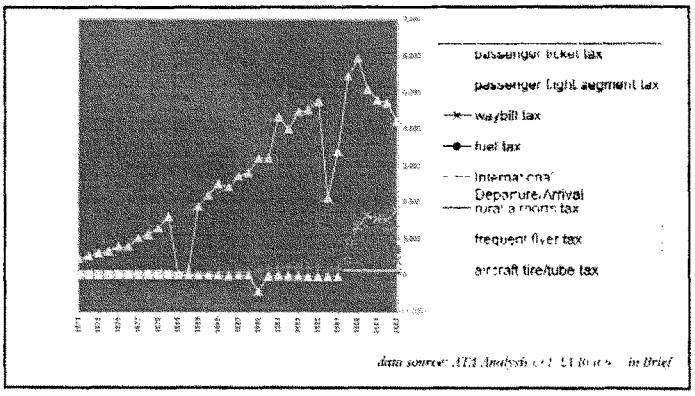
been funded from Trust Fund revenue has fluctuated from year to year from 0% to 100% depending on Congressional Action.[7] Trust Fund revenue is currently supported by ten dedicated excise taxes:

- 7.5% tax on the price of domestic airline tickets
- 7.5% tax on the value of awards or reduced-rate airfares (frequent flyer tickets)
- 7.5% tax on the price of domestic airline tickets to "qualified rural airports"

(flight segment fees do not apply if this tax is levied)

- $3 on each flight segment, indexed to inflation starting in 2003[8]
- 6.25% tax on the price charged for transporting cargo by air
- $0.043 per gallon tax on commercial aviation jet fuel
- $0.193 per gallon tax on general aviation gasoline
- $0.218 per gallon tax on general aviation jet fuel
- $13.40 tax on international arrivals, indexed to inflation[9]
- $13.40 tax on international departures, indexed to inflation

Figure 1: Airport and Airway Trust Fund Revenue by Source[10]



[7] Federal Aviation Administration, Airport and Airway Trust Fund (AATF), 2004 (photocopied).

[8] In 2004, the flight segment fee increased to $3.10.

[9] In 2004, the International Departure and Arrival Taxes were $13.70.

[10] There have been structural changes in the AATF since its inception, creating and eliminating certain types of taxes; all types of taxes have not necessarily been in effect every year.

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As one can see from the chart in Figure 1, since its inception, there have been fluctuations in Trust Fund revenue. Minor fluctuations are likely the result of economic cycles, however, major fluctuations can be attributed to external factors including policy decisions. From 1981-1982, the *Airport and Airway Redevelopment Act of 1970* expired causing the authority to transfer revenue from the excise taxes to the Trust Fund to lapse and in 1996 the ticket taxes expired awaiting congressional action on FAA reauthorization (which included the authority to collect the tax). These fluctuations are the result of policy actions, or inaction, that affected the treatment or collection of revenue and not necessarily the general availability of the funding from the source. Smaller fluctuations are more likely source based rather than policy based as can be seen as a result of temporary declines in air travel, including those as a result of the 1991 Gulf War and the September 11 terrorist attacks, the subsequent war in Iraq, and the international outbreak of Sudden Acute Respiratory Syndrome (SARS). However, as the fluctuations have been temporary in nature, the structure of the Trust Fund, permitting structural surpluses, has allowed funding for aviation programs to continue with steady funding levels.

The percentage of the FAA operations that is funded from Trust Fund revenue (and consequently the amount of Trust Fund revenue that is expended) is determined by Congress and has been subject to a number of policy and statutory restraints. From 1982 to 2000, Trust Fund based funding of operations was limited by tying it to levels of capital investment funding. Under the *Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR 21)*, specific limitations were put on distribution of Trust Fund revenues specifically requiring that the Airport Improvement Program (AIP) and Facilities and Equipment (F&E) receive Trust Fund allocations under a formula before an allocation for operations is made, and data from 2004 to 2012 (projections) are based on the FY05 President's budget. The projected percentage of funding from the general fund is limited by the President's proposed cap of 13% of operations, which represents historically low levels.

The question of appropriate use of the Trust Fund is not new. From 1973 to 1976 the Trust Fund was prohibited from financing FAA operations and maintenance. In

1976, Congress capped the amount of Trust Fund revenue available for operations and maintenance and included a penalty clause, which remained in place until 1990. In 1984, the annual appropriations bill specified that only general treasury funds would be used for FAA operations. In February of 1999, the General Accounting Office responded to an inquiry from Representative Frank R. Wolf, then Chairman of the Transportation and Related Agencies Subcommittee of the House Appropriations Committee, who asked the General Counsel's office to review the legislative history and advise whether the Airport and Airway Trust Fund was created solely to finance aviation infrastructure.

The GAO isolated several pertinent parts of the Act, specifically referencing section 208 (f) (1) (B) which stated that Trust Fund balances could be used for "planning, research and development, construction or operation and maintenance of - (i) air traffic control, (ii) air navigation, (iii) communications, or (iv) supporting services for the airways system." The GAO concluded in its response to the inquiry:

> *The trust fund as it was enacted in 1970 was not created solely to finance aviation infrastructure. Throughout its history, it has financed some non-infrastructure expenses, such as administrative expenses incident to the administration of the airport development program and research and development. With the exception of the time period during fiscal years 1973-1976, it has also funded some costs of maintenance and operation of air navigation facilities.*[11]

While earlier debates focused on whether the Trust Fund could be used to fund portions of FAA operations, more recent debates focus on whether the Trust Fund should provide the sole source of funding for FAA operations. This dramatic shift in how the Trust Fund is viewed with regard to operations funding has sparked recent debate about the long-term viability of the Trust Fund.

In November of 2004, Chief Operating Officer of the FAA Air Traffic Organization Russ Chew stated that the amount available from the Aviation Trust Fund is falling, and increasing pressure on the General Fund means top-up money will be harder to

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[11] Robert P. Murphy, General Counsel, General Accounting Office, Correspondence (12 February 1999).

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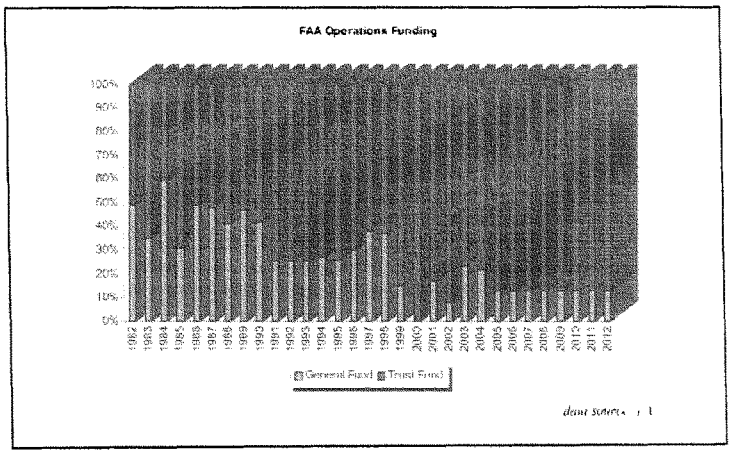
justify.[12] This treatment of a General Fund contribution as "top-up" or extra funding for operations illustrates a new philosophical view of how the Trust Fund is to be treated with regard to operations funding. Further evidence of this philosophical shift is seen in press coverage of FAA funding issues in late 2004. Ken Mead, Department of Transportation Inspector General, said, "When trust-fund revenues are less than the FAA budget, the President's proposal and Congress' appropriation can make up the gap with money from the general fund, allocation of trust-fund surpluses built up in previous years, or a combination of both."[13] Russ Chew was reported as saying that in order to match revenue predictions the ATO operating budget would have to be reduced by 21 percent by 2009.[14]

Throughout the Trust Fund's history the revenues have routinely exceeded allocations from the fund, creating large surpluses causing the administrations and lawmakers to consider options available for reducing the aviation trust fund balance as reflected in GAO studies in 1988 and as recently as 2003.

Figure 2: FAA Operations Funding by Source



12 Adrian Scofield, "Chew Says More Cost Controls Needed to Match Revenue Drop", *Aviation Daily* (5 November 2004).

13 David Bond, "Collision Course: FAA's Trust Fund Isn't What it Used to Be, but Airlines Want Cost Reductions - Not a Fix" *Aviation Week and Space Technology* (22 November 2004).

14 "Chew Says More Cost Controls Needed to Match Revenue Drop" *Aviation Week's The Weekly of Business Aviation* (8 November 2004).

The Public Interest

The division of funding between the Trust Fund and the general fund is more than a question of availability of resources, although the traditional surpluses in the aviation trust fund have provided an attractive option during periods of federal deficits. Rather this is a question of appropriate allocation of costs. This poses a more complicated set of issues revolving around the fundamental question, "who are the users of the system?" An overly simplistic view would consider the users to be limited to the aviation industry. Clearly a closer examination is warranted; the air traveler (or shipper in the case of air cargo) is more appropriately defined as the consumer of the airspace services, while the airline or operator provides the traveler with the means by which he is able to consume the service.

The US air transportation infrastructure provides benefits to a much broader constituency than the direct consumer of air transportation. In many cases, an individual may be completely unaware that he has consumed an aviation service. Our robust and vital air transportation network is present in the day-to-day lives of nearly all Americans. From mail delivery to fresh produce the aviation network permeates our lives. The concept of protecting public safety through aviation goes beyond the prevention of aircraft accidents as it extends to protecting our borders, combating wild fires, national defense and law enforcement. Whether or not an individual is a direct consumer of air travel, all of the residents of the United States benefit from our national airspace system.

In evaluating the public interest in the air transportation infrastructure, one cannot ignore the economic benefits it provides. According to the United States Congress:

> *The total impact of civil aviation on the United States economy exceeds $900,000,000,000 annually and accounts for 9 percent of the gross national product and 11,000,000 jobs in the national workforce. Civil aviation products and services generate a significant surplus for United States trade accounts, and amount to significant numbers of the Nation's highly skilled, technologically qualified work force.*[15]

This is not to say that the air traveler or air cargo user should not bear a significant

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[15] HR2115, *Vision 100- Century of Aviation Reauthorization Act*, (2003).

portion of the cost of operating and maintaining the system, but rather they should not be required to fund the entire cost as there is a portion of the costs that is clearly in the public interest and therefore appropriately funded by the general treasury. The concept of allocating costs to the public sector is neither new nor has it necessarily been a partisan issue. In 1978, under President Carter, and in 1986, under President Reagan, the FAA produced studies attempting to segregate the activities of the FAA that are in the public interest.[16] The reports did not agree entirely on the appropriate distribution of costs, particularly with regard to the cost of regulation, however there is considerable agreement on the major provisions as well as the underlying concept. The 1986 report stated:

> *In the course of meeting its legislated responsibilities, the FAA performs a certain number of tasks which benefit not only the aviation community, but also the public at large. The costs incurred in performing such tasks should not be allocated to any particular private sector aviation user group, but rather should be assigned to the public sector.*[17]

Both the 1978 and 1986 studies identify five categories of expenditure that should be allocated to the public sector. There is consensus between the reporting administrations over the first three items identified as:

1. The provision of air traffic control services at low activity airports. These towers are defined as those that fall below the cost-benefit formula that would warrant continued operation by either FAA staff or FAA compensated contractors. The report argues that the towers are kept open by Congressional action and therefore operate primarily to benefit the public interest and not the system users.

2. The use of FAA services by the military.

3. The use by non-aviators of weather data collected by the FAA.

The fourth item, the benefits received by the public from the FAA's safety, medical, and environmental regulatory programs, is considered fully public in the Carter

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[16] Federal Aviation Administration, *Airport and Airway Costs Allocated to the Public Sector 1985-1997*, (NTIS, Springfield, VA) 1986.

[17] Ibid.

Administration report, while the Reagan Administration argues that it is neither a purely public nor purely private sector expense. Instead the 1986 report advocated the use of a distribution formula.

The fifth item in the 1978 report, the operation of Washington National and Dulles International airports, was rejected as a public cost in the 1986 report. As the FAA is no longer responsible for the operation of either airport, the point is moot for the purpose of a current discussion of the allocation of costs to the public sector. The Reagan Administration reported identifies as a fifth category, the costs associated with civilian government use of the airport and airway system.

The consideration of the costs associated with the identified categories extended beyond operations to include the costs of facilities and equipment to provide the services. The study did not hesitate to allocate the tangible costs of the services consumed by the public interest to the public sector. The report went further to consider the basic safety service provided by air traffic control, stating that there is "theoretical justification for allocating the costs of these programs to the public at large on the grounds that there is a public interest in avoiding catastrophic loss of life."[18] The report goes on to cite as evidence that the major event leading to the formation of the FAA was a mid-air collision between two airliners over the Grand Canyon forty-nine years ago. Essentially, the argument is that if a major accident is cause for a public response to accelerate the formation of the agency itself, then it stands to reason that the service the agency is to provide is a de facto public service.

This question of public policy and the allocation of costs to the public (general fund) or private (trust fund) sector is an important question that should be evaluated in a comprehensive manner. The use of our airspace and airways has changed considerably in the last 20 years and while the earlier reports provide a starting point, a modern assessment should consider whether there are different elements that should be considered today.

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[18] Ibid.

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The Current Debate: Revenue Issue or Policy Shift?

FAA officials are on the record stating that Trust Fund revenues are declining in discussing budget issues at the end of 2004 and into 2005. While it is undeniable that the Trust Fund experienced a sudden and steep decline from 2000 to 2003, it is equally clear that 2004 shows Trust Fund revenue increasing. In addition, the dramatic increases in Trust Fund revenues in 1998 and 1999 put the fund itself at record highs. One could argue that the decline in 2000, which is unrelated to the terrorist attacks, represented a correction rather than a structural decline. While there is no denying that the Trust Fund revenues suffered a decline during the post September 11 recession, there is no indication that revenues are still in decline. In contrast, FAA forecasts for revenue growth are positive and in 2003, the House of Representatives, Senate, and President were considering various aviation tax holiday scenarios. The Government Accountability Office reported that the financial outlook for the Aviation Trust Fund is positive but suspending all taxes accruing to the Trust Fund would eliminate the Trust Fund's uncommitted balance. The GAO's analysis was based on FAA's aviation forecasts, which were published in November 2002. In its 2003 report GAO stated:

> *Although expenditures exceeded revenues in fiscal year 2002, since its creation in 1970, Trust Fund revenues have generally exceeded expenditures - resulting in surplus (or an "uncommitted balance" as it is usually called). For example, at the end of fiscal year 2002, the Trust Fund's uncommitted balance was nearly $5 billion. The Trust Fund's uncommitted balance represents money against which there is no outstanding budget commitment or authority to spend and, subject to congressional approval, is the amount available to finance FAA accounts in the future. It was also used to offset foregone revenue when the Trust Fund taxes lapsed in 1996 and to fund new airport security requirements resulting from the September 11, 2001 terrorist attacks.*[19]

Ops Accounts vs. Trust Fund Growth

Since the mid 1990's the Department of Transportation Inspector General has been

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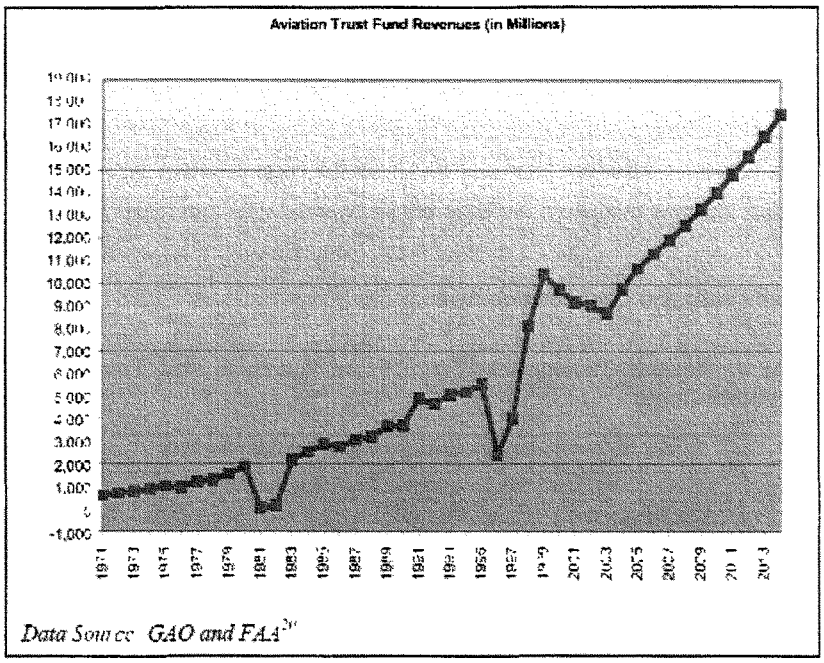
[19] General Accounting Office, *Airport and Airway Trust Fund*, (Washington, DC: GPO, 2003).

Figure 3: Aviation Trust Fund Revenue



highlighting the growth in the FAA operations budget. Trust Fund revenue is the most direct indicator available of the demand placed on the system as it comes directly from the users of the system. So while periodic reviews of the growth in the operations budget have compared it to other FAA budgeted categories, so far the comparisons have not compared the budget growth to the growth in demand and corresponding revenue.

Various reports from the DOT Office of the Inspector General select 1996 as a base year for operations when examining the growth in the budget The reason for selecting 1996 as the base year is not explicitly stated in the reports, however the year corresponds to the first year under legislation establishing a five-year term for the FAA Administrator. Accepting 1996 as a base year and comparing the change in the

[20] Historical data for Trust Fund Revenue obtained from Government Accountability Office reports, projections (2004-2014) are produced by FAA APO-200 for submission to OMB to become part of the President's Projection for Treasury. [online] http://apo.faa.gov/Trust%20Fund%20Website/AATF_ Home.htm#Data. (Accessed November 16, 2004).

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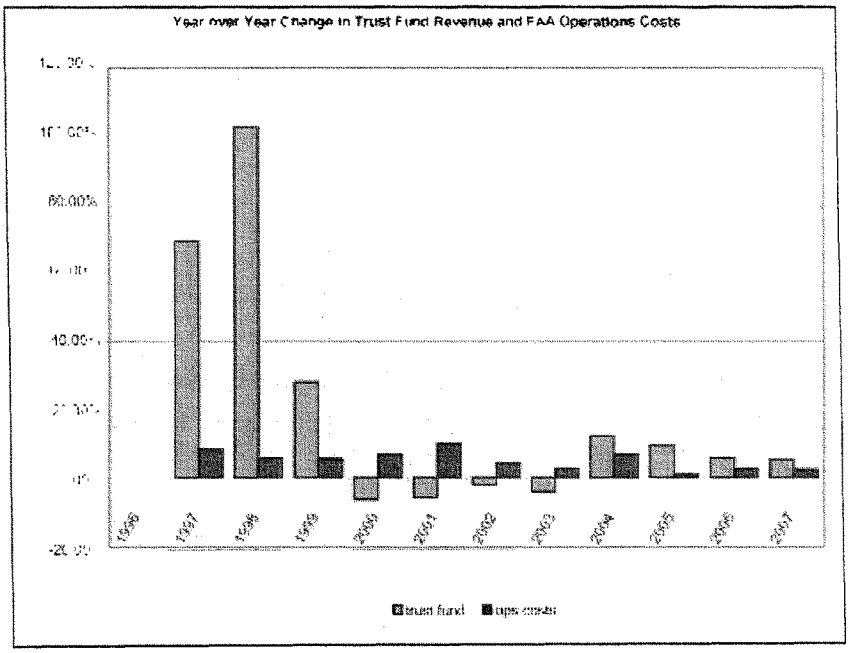
operations budget to the change in the aviation Trust Fund one observes year over year fluctuations that, absent the 2000 correction and 2001-2003 post September 11 decline, the growth in the Trust Fund outpaces the growth in the operations account. That is forecast to continue through 2007, when the taxing authority is scheduled to expire. At that time, Congress will have to consider whether to continue the current funding system or introduce alternatives. Under the current system, both FAA and GAO data illustrate that when revenues are in a normal state (not reacting to a catastrophic event) there remains a healthy relationship between the increase in both operations costs and Trust Fund revenue.

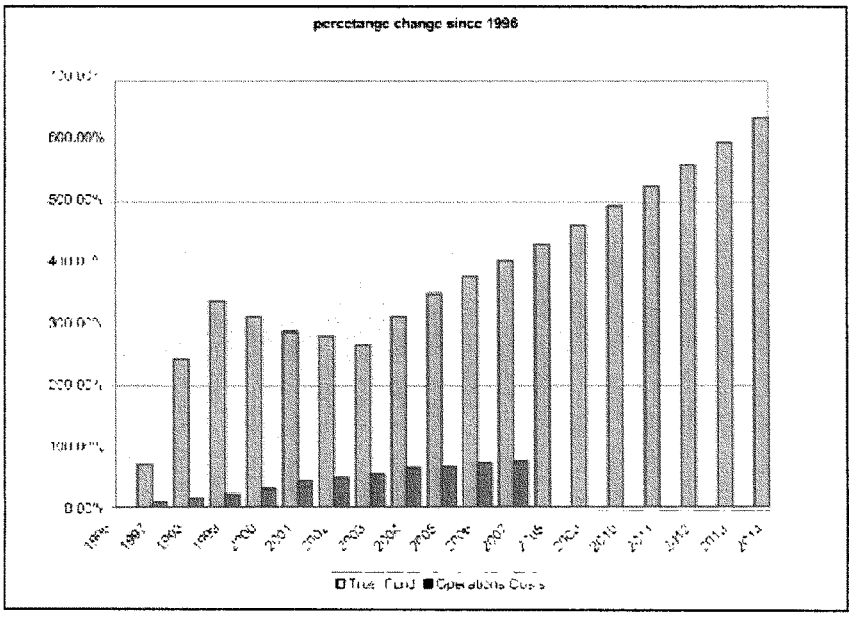
Figure 4: Annual Changes in Trust Fund Revenue and Total FAA Operations Costs



While these have been brief periods during which the Trust Fund was in decline, yet operations cost increased, the overall picture is quite stable and presents an extremely favorable outlook. Rather than a year-by-year analysis, it is instructive to evaluate both costs and revenue growth over a longer term.[21]

However, this approach presents three distinct challenges. First, out-year estimates

Figure 5: Cumulative Trust Fund Revenue and FAA Operations Cost Changes [21]



(2008 and beyond) are based on an estimated percentage increase each year under assumptions of the Office of Management Budget and it is difficult to determine the validity of these assumptions used in making the long term forecast. Second, in 1996 the authority to collect Trust Fund taxes lapsed and was not reinstated until mid-year in 1997. As the revenue levels were depressed in these two years as a result of the policy decision rather than reflecting market conditions, the following year, 1998 showed a corresponding dramatic increase in revenue. It is not that the market con-

[21] The Trust Fund authority expires in 2007, this chart assumes reauthorization of current excise tax and fee structure. Revenue projections are provided by FAA APO-200 as in note 19.

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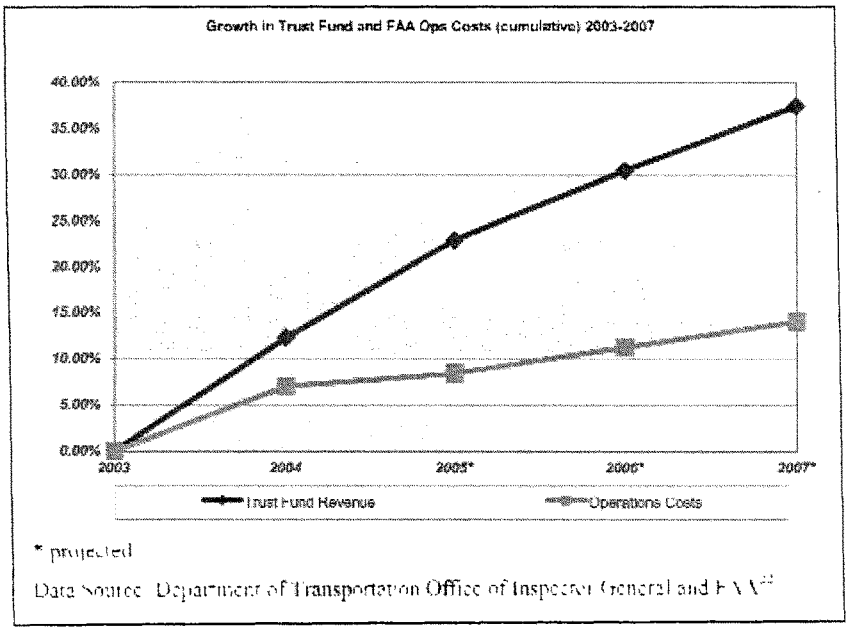
ditions changed, but rather that it was a full year in which revenues were collected. Third, the terrorist attacks of September 11, 2001, caused an increase in operations costs to support security related activities in 2001 and 2002 until most security functions were appropriately transferred out of the FAA. These policy decisions affecting revenue in 1996 and 1997 and expenditures in 2001 and 2002 caused distortions in the model unrelated to market based fluctuations in aviation. Unfortunately, eliminating the years dramatically affected by policy changes and out years only allows for a short-term assessment.

Figure 6: Growth in Trust Fund Revenue and FAA Operations Costs 2003-2007



[22] A single document projecting both operations and trust fund revenue was not available with current data. The delayed recovery from 9/11/2001 substantially shifted trust fund revenue forecasts downward, invalidating earlier projections, therefore the FAA APO-200 FY05 President's Forecast for Treasury is used for projected data as it is both the most current and the most conservative estimates for revenue. Projected operations costs are taken from DOT Inspector General testimony regarding FY2004 Transportation appropriations.

Stability

There is no escaping the conclusion that the expiration of the Trust Fund authority in 1996 followed by the sudden decline post September 11, 2001, and the associated increase in security related spending in 2001 and 2002 has caused a reduction in the uncommitted balance of the Aviation Trust Fund. However, it is the existence of that surplus that allowed the aviation system to continue to operate without raising aviation fees or taxes. The structure of the US system that combines a trust fund contribution with a public sector (general fund) contribution has provided the FAA with a stable source of funding through policy changes, economic fluctuations, and catastrophic events.

It has been argued that the annual appropriations cycle is disruptive to planning, particularly for capital investment, in that the annual FAA budget is not known in advance. In recent years the FAA budget has been unknown even after the fiscal year has begun, while the appropriations process involved numerous continuing resolutions before a final appropriations bill was enacted. While this is not an ideal situation, it introduces no more uncertainty than that which is experienced by organizations financed through other revenue streams that are not guaranteed. One could just as easily argue that the annual appropriation provides considerably more predictability than revenue driven models based on traffic projections considering that if revenue fails to meet predictions it would require more frequent adjustments to planned investment.

FAA data illustrate that while the Airport and Airway Trust Fund suffered a brief but predictable decline as a result of the reduction in air travel post September 11, 2001, it is equally clear that as air travel is increasing, so too is the Trust Fund and continued growth is forecast by the FAA. The question of available resources for FAA operations is limited by policy choices rather than Trust Fund forecasts. The question of Trust Fund allocation and what percentage of FAA operations is appropriately funded from the general treasury vs. the Trust Fund, more so than Trust Fund revenue itself, will determine whether adequate resources are available to meet the demands placed on the system.

24 User Fee Based Models

An Overview

The terms privatization, commercialization, corporatization and liberalization are used somewhat interchangeably and imprecisely in describing broad categories of air traffic service providers under various types of government structures, charging regimes, regulations and ownership. While many different providers share certain characteristics, there is not one common structure that defines the majority of service providers. However, the vast majority of so-called privatized air traffic service providers are in fact not privatized, but rather government owned entities. Detailed information in English is not easily accessible for all providers making comparisons difficult, however this overview provides examples of different frameworks currently in place.

ICAO has published recommendations on appropriate charging mechanisms for international civil aviation. These recommendations are general in scope allowing for adaptation by individual States. In general, ICAO considers that, "providers may require the users to pay their share of the related costs; at the same time international civil aviation should not be asked to meet costs which are not properly allocable to it."[23] In its charging recommendations, ICAO distinguishes between commercialization and privatization. According to the glossary of terms, commercialization is referred to as an approach to management of facilities and services in which business principles are applied, while privatization is it the transfer of full or majority ownership of facilities and services to the private sector.[24] Under these definitions, the US system, structured under the ATO, could be classified as commercialized.

Just as the organizational structures for air traffic control service providers vary, the scope of services provided also varies widely. In the United States, the FAA provides services to both military and civil aircraft and controls both en route and terminal (airport) air traffic. In other countries airports may be controlled by a separate

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[23] ICAO, *ICAO's Policies on Charges for Airports and Air Navigation Services - Seventh Edition*. (Montreal: ICAO,2004).

[24] Ibid.

entity than en route and the civil provider may coordinate with, but remain separate from the military authority. This can be true in both traditional public and corporatized structures. However, in the case of civil and military operations there is a clear trend emerging to consolidate the service provision in order to maximize airspace efficiency, similar to the United States model.

Charging Regimes

ATC providers that utilize user fees as a charging mechanism generally assess one or more of the following types of fees:

- En Route Charge - en route charges are generally determined using a formula that considers the weight of the aircraft and the distance flown, with weight determined by formula and distance determined by either actual distance flown or great circle route distance between departure and arrival point. In the European systems, most countries follow the guidance issued by EUROCONTROL in the document, "Principles for Establishing the Cost-Base for Route Facility Charges and the Calculation of Unit Rates" and revenue collection is facilitated by the Central Route Charges Office. However, each country retains the authority to set its own Global Unit Rate (or Chargeable Service Unit) and there is wide disparity between the rates with Switzerland, the most expensive in Europe in 2004, charging a rate that is nearly three times that of Ireland, with one of the lowest rates.

- Terminal Charges - terminal charges are calculated considering the maximum take off weight of the aircraft and some providers may charge a different rate for foreign registered and domestic registered aircraft.

- Landing Fees - landing fees are general collected and retained by airport operators, which may be entirely separate from the air traffic service provider.

Government Owned Models

Airservices Australia

In 1995, the Australian Civil Aviation Authority split into two separate government bodies, the Civil Aviation Safety Authority and Airservices Australia which is a gov-

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ernment owned corporation providing air traffic control services in upper airspace over Australia and to the Pacific Island Flight Information Region over the Solomon Islands and Nauru as well as air traffic control services at 26 Australian airports. Unlike most European providers, Airservices Australia also provides firefighting services at 17 Australian airports.[25] It is governed by a board of directors appointed by the Minister for Transport and Regional Services. In addition to en route and terminal navigation charges, Airservices Australia also collects fees for aviation rescue and firefighting charges.[26] These fees are assessed if the services are available for use at time of landing or at anytime while the aircraft is in circuit training. En route charges are applied for the entire flight if any part of the flight operates under Instrument Flight Rules.

Airservices Australia also collects the Meteorological Service Charge and the Noise Levy Charge on behalf of other government agencies. All charges are billed to the owner of the aircraft unless liability is assigned through the execution of an Acceptance of Liability for Airways Charges document. In addition to its core functions, Airservices Australia operates a multi-profit center business to sell its services to external customers. Recently the commercial operation was successful in winning bids to take over contract tower services at six FAA locations in the Pacific.

Airservices Australia retains 40% of its profit for reinvestment programs and the government receives a dividend on retained earnings. In 1998 and 1999, the government provided a cross subsidy of $11 million to support below cost pricing at small regional and general aviation airports in recognition of the public interest.[27]

European Structure

ATC corporatization in Europe gathered support as a means for coping with unprecedented European air traffic increases. Corporatization allowed for the systems to introduce new charges to generate additional revenue to fund ATC infrastructure investment by shifting greater portions of the costs onto the users to allevi-

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[25] Airservices Australia, *Corporate Overview: From the Ground Up*, [online] http://www.airservicesaustralia.com

[26] Airservices Australia, *Charges for Facilities and Services*, (January 2005).

[27] Civil Air Navigation Services Organisation, *Corporatisation of Air Navigation Services: A Special Report*, (August 1999).

ate pressures on State treasuries. Sovereign boundaries surrounding relatively small geographic areas led to a complex patchwork of systems and charging structures. A desire for harmonization in regional en route charges led to the establishment of the EUROCONTROL Central Route Charges Office (CRCO). The basic principles for a common system to allow a single charge per flight were adopted by Member States in 1969, implemented in 1971 and the common policy for establishment and calculation of route charges builds on the principles of multilateral agreements effective in 1986. The CRCO also provide billing and collection services for terminal charges to Member States and will provide air navigation billing and collection services to non-Member States on a bilateral basis.[28]

The centralization of fee collection may have provided an impetus for corporatization of air traffic service provision across Europe as the individual providers did not have to establish independent infrastructures for the calculation, billing and collection of charges, yet the States remained free to set the rates of charges within the guidelines specified in multilateral agreements conforming to the EUROCONTROL publication "Principles for Establishing the Cost-Base for Route Facility Charges and the Calculation of the Unit Rates" which specifies the costs that can be considered in determining the costs to be recovered from the users. (See Appendix 1)

The national unit rate is determined by dividing the forecast number of service units into the forecast cost-base for the relevant year. Each flight is then charged based on a formula that multiplies the distance factor, the weight factor and the relevant unit rate. The distance factor is equal to one hundredth of the distance, in kilometers, of a direct route flown between the point of entry to the point of exit in the Flight Information Region (or aerodrome if departing or landing in the airspace). The weight factor is the square root of the quotient obtained by dividing the number of metric tons of maximum take off weight by fifty.[29]

As the unit rate is determined by forecast traffic, an unanticipated downturn in traffic will cause a revenue shortfall, which can be disruptive to planning. In addition,

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[28] Central Route Charges Office, *The EUROCONTROL Route Charges System* [online] http://www.eurocontrol.int/crco/public/standard_page/intro_rcs.html

[29] Ibid.

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this demand-based method necessarily causes unit rates to be higher during periods of low demand and lower during periods of high demand. This methodology substantially increases the likelihood that fees will increase when users are least able to pay, as high demand is indicative of a healthy aviation industry while low demand for air traffic services is reflective of an economic downturn for the industry.

Under the centralized system, the CRCO will calculate, bill and collect fees that represent the total route charge for a given flight and redistribute the fees to Member States based on the portion of the flight with in the State's FIR. While the charge may seem homogeneous to the user, the fees collected by each State may be substantially different even if comparable amounts of services were consumed in each FIR (see Appendix 2). Additionally, as the calculation is based on a point-to-point route and not necessarily the route flown, services may be provided by one State while the associated revenue may be retained by another.

Luchverkeersleiding Nederland (LVNL) - Air Traffic Control - the Netherlands

LVNL is a fully government owned corporation supervised by a board appointed jointly by the Minister of Transport and the Minister of Defense. The restructuring of the LVNL to become independent from the Civil Aviation Administration was a seven-year process during which the option of privatization was considered and subsequently rejected because of the public nature of ATC service provision.[30] LVNL provides civil air traffic control services within the boundaries of the Netherlands Flight Information Region in en route airspace up to 24,500 feet above mean sea level and approach control and tower services at Amsterdam Schiphol, Rotterdam, Maastricht and Groningen airports. Military air traffic control services remain under the jurisdiction of the Ministry of Defense.

Although government owned, the LVNL is subject to strict regulation, reporting and oversight by the Ministry of Transport, which remains politically responsible for aviation safety and setting regulations. In addition, the government regulates capacity and noise related issues.

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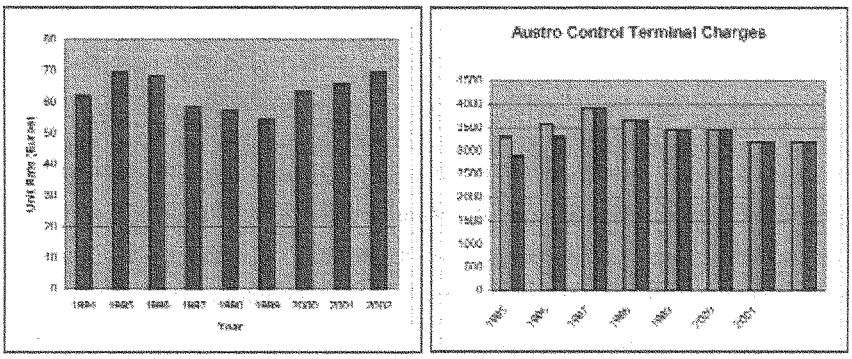
[30] CANSO Corporatisation Report - LVNL (2002).

LVNL has no shareholders and is not permitted to retain or invest any profits. Capital investment is funded through bank loans, revenues are derived from terminal charges collected by the airports authorities and en route charges collected by the EUROCONTROL Central Route Charges office. Fees for ATC service provision are proposed by the supervisory board and subject to approval by the Ministry of Transport.

Austro Control GmbH

Austro Control GmbH is a limited liability company, founded in 1993, for which the Austrian Government retains 100% of the shares. Austro Control funding is derived from en route and terminal charges as well as a contribution from the government paid on a cost recovery basis for duties executed on behalf of the government.[31]

Figure 7: Austro Control ATS Charges



Data source: Austro Control, GmbH

[31] CANSO Corporatisation Report - Austro Control GmbH (2002).

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The fluctuations in charges, particularly in the unit rate for en route charges, may have an adverse effect on system users by introducing volatility into the user cost structure. This effect may not be recognized as quickly in the case of Austria as the distance flown traversing the airspace is small.

Skyguide

Skyguide provides air traffic control services to civil and military aircraft in airspace over Switzerland and designated portions over neighboring countries and at Zurich, Geneva, Bern and Lugano airports. Corporatization of air traffic control in Switzerland is not a new concept as primarily state owned corporations have operated air navigation services in Switzerland since 1921. The ownership of the Swiss ATC provider has undergone several reorganizations and government ownership has fluctuated from a low of 51% to the current high of 99.85%. In 2001, Swisscontrol underwent not only a name change to Skyguide, but also added the responsibility for military air traffic control.[32] Currently, it is a non-profit organization for which the Swiss government holds 99.85% of the shares with the remaining 0.15% owned by other public entities in aviation, such as airports.

The system is funded through en route and terminal charges. The unit rate is set by Skyguide and subject to approval by the Ministry of Transport. Revenue is derived from en route charges, collected by EUROCONTROL's Central Route Charges Office and terminal charges collected by the airports, with the exception of Lugano where Skyguide is the direct collector of the charges. Skyguide's investments are financed through cash flow as well as private bank loans and loans from the Swiss government.

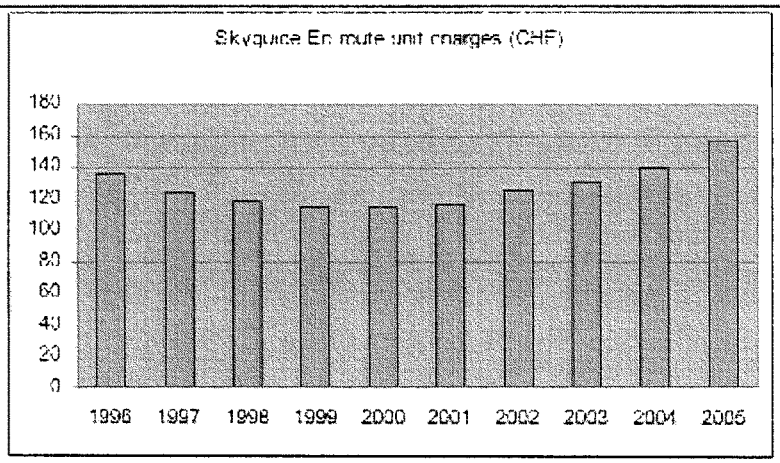
The Skyguide restructuring promised, and delivered, initial reductions in route charges, which resulted in pressures to achieve cost reductions. Unfortunately, Skyguide suffered a catastrophic mid-air collision between two aircraft under its control. Subsequent investigations have identified a series of cost cutting measures that weakened backup systems on both a technological and procedural level. The air

[32] CANSO Corporatisation Report - Skyguide (2002).

traffic controller involved was subsequently murdered by a family member of a passenger killed in the crash and is unable to provide additional insight into the systemic breakdowns that lead to the catastrophic loss of life.

As of their 2002 report, the reductions in the unit costs immediately following the restructuring from Swisscontrol to Skyguide were anticipated to return to pre-restructuring levels by 2003 and continue to climb in the near future. Skyguide currently has the highest route charges in Europe.

Figure 8: Skyguide Route Charges



Data Source: Skyguide

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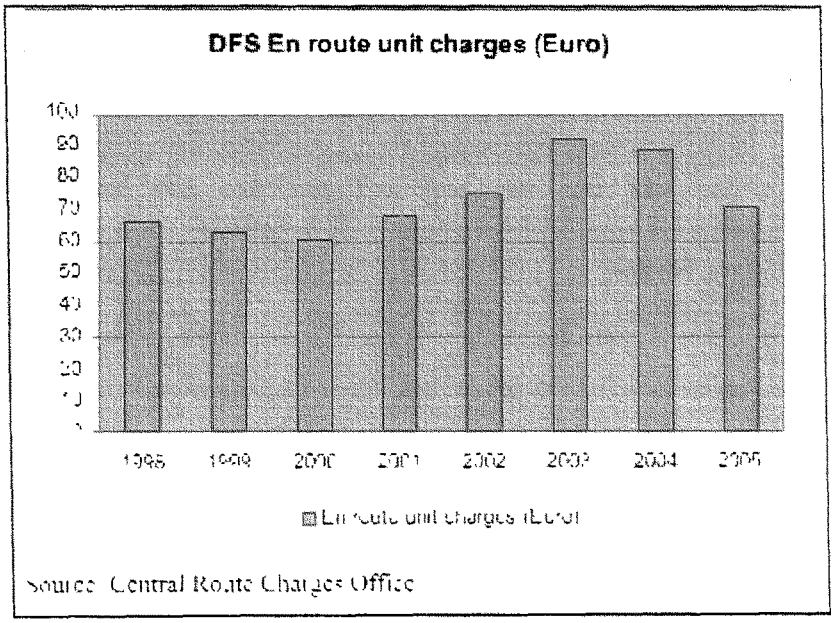
Deutsche Flugsicherung GmbH - DFS (Germany)

DFS, created in 1992, began operation as a wholly state owned corporation in 1993 to provide air traffic control services in Germany. Currently, DFS provides air traffic services to civil and military aircraft in en route airspace over Germany and at 17 international airports. The integration of military air traffic control has provided DFS with increase flexibility in the use of airspace. DFS attributes this to the corporatization.[33] The Ministry of Transport decides how much profit, if any, is retained by the state or deposited into DFS capital reserves.[34] Unlike other state owned providers, DFS is required to make a profit. Like other providers using the European charging regimes, rate reductions in the late 1990's proved unsustainable in the face of declining traffic and subsequently unit rate charges experienced dramatic increases.

Figure 9: DFS Route Charges



[33] Statement of Deiter Kaden, Chief Executive Officer and Chairman of the Board of Managing Directors DFS Deutsche Flugsicerung GmbH, before the U.S. House of Representatives, Subcommittee on Aviation (20 April 2005).

[34] CANSO Corporatisation Report - DFS (2002).

The corporation is headed by a Chief Executive Officer, supported by three managing directors and has a supervisory board consisting of six elected employee representatives and six representatives of the owner (the Federal Republic of Germany).[35] It is clear from DFS documents that the government structure prior to corporatization did not allow flexibility in either personnel or procurement processes and that flexibility was not available under other statutory provisions.

Europe is currently in the process of a sweeping effort to harmonize ATC service provision driven by a concept of operations that would allow European airspace to operate more like the US structure and move toward efficiencies currently achieved by the FAA, as European ATM costs are considered high in relation to the US.[36] The implementation of the Single European Sky will eliminate sovereign boundaries for Air Traffic Service provision and allow privatized providers to bid for services in any State. In order to take advantage of that opportunity, DFS has implemented a privatization plan in which the government will sell 74.9% of DFS to private investors to be completed in 2006.

Supranational Providers

EUROCONTROL

EUROCONTROL's primary function as the European Organization for the Safety of Air Navigation is to facilitate the development of a pan-European air traffic management system. It works with States and providers toward harmonization and is not currently working to supplant existing providers. EUROCONTROL has 34 Member States and operates one air traffic control center controlling the upper airspace over Belgium, the Netherlands, Luxembourg and part of Germany. It is currently in the process of developing a second center to control the upper airspace over eight States in Central Europe.

The Maastricht center became operational in 1972 and while it is part of the EURO-

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35 Ibid.

36 EUROCONTROL Performance Review Commission, *A Comparison of Performance in Selected US and European En-Route Centres*, (May 2003).

34
CONTROL organization, it is managed and financed solely by the four participating States.[37] The costs for services are added to the participating States' national cost basis and incorporated into the route charges.

Public Private Partnership

Overview

The term public-private partnership is broadly used to describe any collaboration between the public and private sector. Public-private partnerships exist in many countries and across industries. While the PPP can take many forms it is most commonly seen in large construction projects where the private sector provides initial financing for capital projects and recoups the investment either from a designated revenue stream (like a highway toll or special taxation district) or rents the project back to the public sector.[38]

National Air Traffic Services (NATS) - United Kingdom

In 1996, National Air Traffic Services was corporatized as a wholly owned company under the Civil Aviation Authority in preparation for a proposed privatization. The government considered several options, including privatizing the system as a regulated monopoly, a non-profit trust, a public corporation or under the Private Finance Initiative. In 1999, it was decided to proceed with a public-private partnership that was completed in 2001. The initial structure provided the government with a 49% share and veto power on key strategic issues and retention powers to deal with national emergencies and to ensure public service obligations are met. A 5% stake was held for employees and 46% stake was sold to a consortium of seven British airlines.[39]

Under this structure civil and military operations were divided and military air traffic control fell under the Ministry of Defense. While most providers consider civil-military integration to be a critical step in enhancing efficiency, the introduction of

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[37] EUROCONTROL, *Frequently Asked Questions*, [online] www.eurocontrol.int/muac/public/ faq/FAQmaastricht.html

[38] BBC News, *What are Public Private Partnerships?* (12ebruary 2003).

[39] CANSO Corporatisation Report - NATS (2002).

the PPP necessitated the separation of these services that had been integrated in the government model.

The NATS model differs from other European providers in that it is also subject to an economic regulator. Seventy-five percent of NATS income is derived from en route charges calculated under the EUROCONTROL model, other revenue is derived from aerodrome navigation charges collected from aircraft operators or charges paid by the airport company.

NATS has experienced considerable financial difficulties from the beginning of the privatization process. After the Airline Group was selected as the private sector partner, it notified the government that it could not afford the price it had bid and reduced the initial proceeds to the government by £87 million. The initial structure caused the NATS debt to more than double from £330 million to £733 million. The initial projections all assumed continual growth in air traffic and facing an almost immediate downturn compromised the financial viability of NATS while simultaneously threatening the solvency of its private partner - the airline consortium.[40] This structure proved particularly fragile as the both NATS and the Airline Group are adversely affected by the same externalities.

Less than a year after the creation of the PPP, NATS required significant financial restructuring in order to avoid alternative outcomes perceived as less desireable. These potential outcomes included:

- Putting the company into administration, which would threaten the equity stake of both the Government and the Airline Group and put the banks that had financed the PPP at considerable risk.
- Returning the company to public sector ownership.
- The banks curtailing access to capital, forcing NATS to shed parts of the business not related to meeting the statutory obligation and limiting future investment.

The composite solution required concessions from all parties and took over 18 months to complete, eventually resulting in a restructuring of the ownership equity

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[40] National Audit Office, *The Public Private Partnership for National Air Traffic Services, Ltd: Report by the Comptroller and Auditor General* (House of Commons: 24 July 2002).

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and new investment of £65 million from the UK government to match the £65 million investment from a new equity investor, BAA plc. BAA plc joined as a minority shareholder in NATS with voting rights of less than 5% and the right to appoint two non-executive directors to the 17 member board of NATS. In achieving the restructuring the Airline Group reduced its equity share to 41.94% and the Government reduced its share to 48.87% in order to afford BAA plc a 4.19% share in exchange for its investment. Although the government increased its investment, it reduced rather than increased, its equity stake.

Notwithstanding the substantial government infusion of cash into NATS, this restructuring is not purely a government bailout. The UK government refers to the PPP restructuring as a "composite solution" as all parties contributed to the solution, many of whom made considerable concessions.

- The Government invested £65 million on the same terms as BAA plc, tolerated a dilution of their equity stake, and provided a temporary £30 million loan facility.
- BAA plc invested £65 million and accepted constraints on voting rights.
- The Civil Aviation Authority agreed to relax the economic regulation and price caps, allowing NATS to raise its prices automatically to recover a portion of lost revenue due to traffic decline. These concessions are expected to cost airlines £100 million between 2003 and 2010.
- The Airline Group enlisted support from airlines for higher prices and accepted dilution of their equity stake.
- The banks agreed to relax some loan terms and reinstate the investment facility.
- NATS cut costs by £170 million, agreed to heavier penalties for delays and more financial reporting to the CAA.[41]

While the financial picture for NATS is substantially more robust than the previous structure, the organization continues to carry heavy burdens for debt service. NATS's 2004 financial reports indicate secured and unsecured loans totaling £114,157,000 in 2004 up from £107,899,999 in 2003 at an interest rate of 8.5% repayable in 2031.

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[41] National Audit Office, *Refinancing the Public Private Partnership for National Air Traffic Services: Report by the Comptroller and Auditor General* (House of Commons: 7 January 2004).

The NATS financial crisis following the transition to PPP should be ascribed to overly optimistic forecasts, not withstanding the September 11 downturn. A dispassionate analysis reveals that the traffic downturn began well before the terrorist attacks on the United States as evidenced by the change in the offer by the Airline Group prior to completion of the arrangement. This change based on traffic forecasts should have given pause to those involved in the structuring of the PPP. Additionally, UK air traffic levels are historically volatile, having experienced greater and more abrupt traffic fluctuations than it did as a result of September 11, 2001.

The overly optimistic views that led to the fragile financial structure of the NATS PPP are indicative of difficulties being faced by most corporatized or privatized providers. According to the Civil Air Navigation Services Organisation (CANSO) there are fundamental weaknesses in the charging mechanisms, in that the current Air Traffic Management finances are not designed for a downturn.

The Privatized Model

Overview

Under a fully Privatized model, all assets are transferred to the private company. In the Canadian privatization, the national air navigation system, as well as air traffic control equipment, was sold for CDN $1.5 billion to NAV CANADA. In addition to the public policy questions, the sale of infrastructure assets raises questions regarding the obligation of system user to bear the cost of that transfer. Ostensibly, infrastructure assets are initially purchased with government resources obtained through previously paid aviation taxes. Through privatization schemes a private sector provider will utilize debt financing to purchase the system from the government. The debt is then repaid through future user fees, essentially requiring the users to pay for through fees, that which they had already purchased through aviation taxes. If aviation taxes are not allocated solely for aviation purposes and instead serve as general revenue, as is the case in many countries, then the purchase price is reimbursement to the taxpayers and not necessarily double billing to the aviation users.

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NAV CANADA

NAV CANADA was established in 1996 as a non-share capital corporation and is a fully privatized provider of air traffic control services. NAV CANADA purchased the air traffic control business and assets of Transport Canada for CDN $1.5 billon. The impetus for commercialization in Canada was in response to concerns that the Canadian government operated system was "under funded, procurement practices were slow and costly, and the employment practices were inflexible."[42]

NAV CANADA is governed by a 15 member Board of Directors plus a President and Chief Executive Officer. The financing plan includes provisions for a variety of term bank debt, commercial paper, and hedging instruments. NAV CANADA entered into a CDN $3 billion credit arrangement with a syndicate of banks to provide the initial funding for the company, NAV CANADA states that it is "by and large responsible for establishing and regulating its own safety practices" and that the current framework essentially allows for self-regulation rather than an economic regulator.[43] The Civil Air Navigation Services Commercialisation Act allows the company to recover its costs and prudent financial reserves through user charges. Like other providers, user charges are based primarily on a weight distance formula, subjecting revenue to fluctuations in conjunction with traffic changes. In addition, it is financed through bond markets with CDN $2.2 billion in fixed income securities.[44] NAV CANADA maintains a rate stabilization account so that temporary fluctuations in traffic do not dictate changes in user charges. A surplus in the rate stabilization account is treated as a liability as it is returnable to users through reduced future charges and a negative balance is treated as an asset as it is recoverable through increased future charges.

At the end of 2001, the rate stabilization account had a positive balance of CDN $75 million, but by the end of 2003, the account had a negative balance of CDN $116

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[42] Civil Air Navigation Services Organisation, *Corporatisation of Air Navigation Services: A Special Report*, (August 1999).

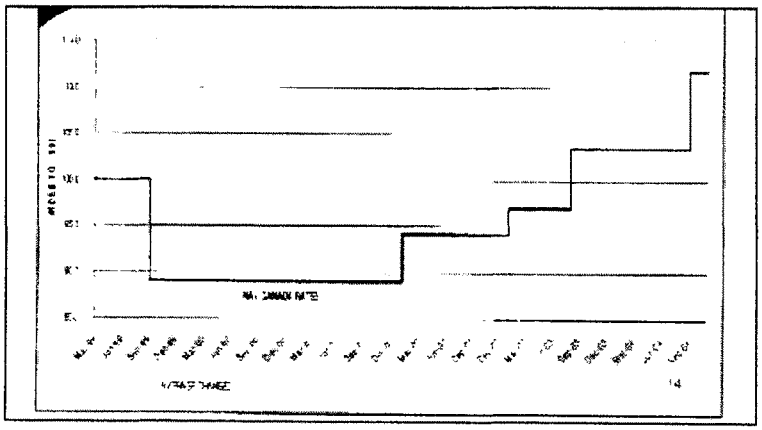
[43] Ibid.

[44] *Statement of John Crichton, President and Chief Executive Officer NAV CANADA*, before the House Aviation Subcommittee, (20 April 2005).

million,[45] even though NAV CANADA had increased charges three times between the end of 2001 and the end of 2003[46], provoking strong reactions from system users. Air Canada appealed one of the fee hikes, describing the fee increase as "completely out of touch with industry realities" and that fee increases "continue unabated on their unstable, upward spiral."[47] Giovanni Bisignani, CEO of the International Air Transport Association joined the criticism of NAV CANADA stating that it "is no longer delivering value for money" and called for increased government regulation of "private monopolies."[48]

Recently, NAV CANADA has taken advantage of a capital leasing transaction that provided CDN $56 million increase in net present value. Under this arrangement NAV CANADA entered in to lease/leaseback transactions of the company's air navigation facilities with no real transfer of assets.[49] Like NATS, NAV CANADA is heavily burdened with debt and incurred interest payments of CDN $136 million in fical year 2004.[50]

Figure 10: History of NAV CANADA Rate Charges



Data source: NAV CANADA

[45] NAV CANADA, *Management's Discussion and Analysis on Form-51-102F2*, (12 April 2005).

[46] NAV CANADA, *Annual report 2004:Serving a World in Motion (2004).*

[47] Adrian Schofield, "CTA Dismisses Appeal Against Nav Canada Fee Hike" *Aviation Daily* (24 November 2003).

[48] Nicolas Van Praet, *"Global Airline Chief Slams Canadian Policies: Fee Gouging Alleged by Iata's CEO" CanWest Interactive* (10 September 2003).

[49] NAV CANADA, *Annual report 2004:Serving a World in Motion (2004).*

[50] Ibid.

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Stability

User fee based systems, regardless of corporate governance, introduce considerable instability into the funding structure for air traffic control. Some structures have mechanisms in place, like Canada's rate stabilization fund, to mitigate the effects of traffic fluctuations. However, this mechanism proved inadequate when the provider encountered multiple externalities. Traffic decline following September 11, 2001, followed by the SARS scare in Toronto compounded by the bankruptcy filing of the nation's largest air carrier depleted the reserve fund, forcing a series of rate increases.

The instability of user fee based systems is compounded as experience shows that Air Traffic Service providers have opted to increase fees when their users can least afford it. In this way, the Air Traffic Service provider is in competition with the aviation industry during periods of economic downturn. That is not to say that the providers will not be in competition with the industry during times of strong growth. History has shown that during periods of industry strength, airlines tend to regard providers as over collecting fees and the pressure for rate reductions rather than infrastructure investment is as aggressive as the cry for rate cuts during a decline. In its 2003 report, the Regulatory Policy Institute found:

> *One of the most contentious issues in ATM is the allocation of risk, particularly of financial risk associated with traffic volatility. Current arrangements are manifestly deficient in this regard, and can give rise to significant short-term movements in charges that bear no relationship at all to movements in the cost of service provision.*[51]

Privatization or corporatization of air traffic control services is frequently marketed as providing stable sources of funding, as the providers have access to commercial markets, and as a means to introduce market based incentives to increase system efficiency. Experience has shown that the structures are primarily designed for continued traffic growth and cannot be sustained in a market downturn, and there is

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[51] National Audit Office, *Refinancing the Public Private Partnership for National Air Traffic Services: Report by the Comptroller and Auditor General* (House of Commons: 7 January 2004).

considerable risk that providers will become overburdened with debt. Costs associated with debt servicing can divert resources away from both service provision and infrastructure investment. Further, the EUROCONTROL Performance Review Commission found:

> *The present full cost recovery regime does not provide incentives to deliver performance and to be responsive to user needs beyond levers normally available in the public sector. With the current system, airspace users are bearing most if not all, of the business risks. On theone hand, if demand is higher than expected or if the planned capacity is not delivered, airspace users will incur higher delays. On the other hand, if demand is lower than expected or actual costs are higher than planned, the airspace users will incur higher charges.*[52]

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[52] EUROCONTROL Performance Review Commission, *An Assessment of Air Traffic Management in the Calendar Year 2002* (May 2003).

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Conclusion

Air Traffic Control service provision, once the almost exclusive domain of traditional government bureaucracies, has undergone tremendous restructuring worldwide. It is clear from the myriad of structures that no "one-size-fits-all" model exists. The statutory and constitutional constructs within different States may dictate necessary structures, but those limitations may not apply to even neighboring States. In determining the ideal framework for financial structures and corporate governance, the provider and stakeholders should consider the fundamental principles necessary to achieve clearly defined goals.

Policy makers should not assume that the barriers to achieving desired goals exist uniformly between States or that the structural framework for one provider is necessarily ideal for another operating under a different governing structure. For example, corporatization was desired in Germany because the civil service structure did not allow for flexibilities in personnel and procurement, but the United States was able to achieve the flexibility it desired through a statutory change without introducing the financial risks associated with corporatization.

A reliable and robust air traffic control system is a critical component in ensuring a national economy is able to maximize the benefits provided by a vigorous aviation industry. As air traffic control modernization in particular requires long term planning, a stable and predictable funding mechanism is required. Any funding mechanism constructed for the purpose of air traffic control service provision must meet the fundamental tests of providing both adequate and stable resources.

Appendix 1: EUROCONTROL Cost Base

Source: EUROCONTROL Central Route Charges Office

In establishing the cost base for establishing national route charges, EUROCONTROL advises Member States to include the following:

Investment costs:

- Amortization of fixed assets - including equipment, buildings, land, basic software and application software
- Amortization of intangible assets
- Cost of Capital - including cost of capital incurred during the pre-operations phase
    - Interest paid to providers of debt capital
    - Cost of capital applied to equity

Operating costs:

- Rental for land or transmission lines
- Rentals costs of land, buildings, other facilities and applicable taxes
- Cost of utilities
- Rent for Aeronautical Fixed Telecommunications Network (AFTN)
- Total operating costs of other operational and technical support facilites, administrative support, legal, consultancy and audits

Staff costs:

- Actual costs of staff including trainees, supervisors, support staff, including pension and insurance costs

Air Traffic Management Costs:

- Air Traffic Services

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- Air Traffic Flow Management
- Airspace Management

Communication, Navigation and Surveillance Costs:

- Costs of communications, navigation and surveillance facilities including Global Navigation Satellite Systems

Costs of basic and advanced training

Costs in respect of studies, tests and trials

Administrative costs

Aeronautical Information Service

MET Costs (meteorological services)

Search and Rescue costs

Appendix 2: National Unit Rates

Member State	Unit Rate - EUR
Belguim-Luxembourg	83.83
Germany	71.49
France	60.58
United Kingdom	81.50
Netherlands	53.69
Ireland	31.09
Switzerland	86.11
Portugal - Lisbon	49.02
Austria	68.65
Spain - Continental	71.95
Spain - Canary Islands	66.05
Portugal - Santa Maria	14.98
Greece	36.84
Turkey	28.50
Malta	31.74
Turkey	28.50
Malta	31.74
Italy	69.57
Cyprus	34.36
Hungary	35.10
Norway	60.79

46 Denmark	56.93
Slovenia	70.04
Romania	40.97
Czech Republic	28.25
Sweden	50.75
Slovak Republic	41.33
Croatia	50.08
Bulgaria	52.83
FYROM	64.28
Moldova	35.47
Finland	38.25
Albania	46.71
Bosnia Herzegovina	47.01

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Statement of
James C. May
President and CEO
Air Transport Association of America, Inc.
Before the
Subcommittee on Aviation
Committee on Transportation and Infrastructure
United States House of Representatives
May 4, 2005

Mr. Chairman and members of the Subcommittee, thank you for inviting me to appear before you today to offer the Air Transport Association's (ATA) observations on the financial condition of the Aviation Trust Fund and alternative mechanisms for financing future needs. While we are only at the opening stages of what will surely be a robust debate on how to "fix" the Trust Fund, it is never too soon to identify the drawbacks of the current scheme and begin the discussion of potential solutions. The airlines have a direct interest in this debate because we provide well over ninety percent of the revenue for the Trust Fund [CHART 1], even though we account for roughly only two-thirds of the operations. And we pay more: once in the form of taxes and fees, and again in future delay costs when Trust Fund monies are not properly invested in system modernization.

We have an appreciation for the enormous challenge facing the Federal Aviation Administration (FAA) because it is all too similar to what the airline industry has been struggling with for the past four years. Revenue shortfall in the billions? We know all about it. Outdated "legacy" systems? We've been there. High labor costs? We feel your pain. And having grappled with these tough issues, we know that the next few years will not be easy. But just as the airlines have responded to the challenge by shedding more than one out of six jobs, restructuring employee compensation and

benefits, changing work rules to increase productivity, parking inefficient and expensive-to-maintain equipment, and consolidating facilities and operations, the FAA will need to take meaningful steps to improve efficiency .

I. State of the Trust Fund – How We Got Here

For too long, the Trust Fund has been viewed as a bottomless pot of money that is easily replenished by taxes on commercial aviation. To an extent, the Trust Fund is suffering not so much from a lack of funds as from an abundance of demands on those funds. Everyone, it seems, wants his slice, and over the years the Trust Fund has been carved up to the point where there is no longer enough left to do what it was originally intended to do: *expand and improve the national airport and airway system.*[1] We've reached the point where less than 20 percent of annual appropriations from the Trust Fund is made available to expand capacity or improve the efficiency of the system. The rest goes to operate and maintain the existing system, cover administrative costs and to fund various set-asides that have at best a tangential relation to the national system. [CHART 2]

In the past few years, we have seen the Trust Fund go from allowing significant surpluses to accumulate to drawing down the balance of the Trust Fund to the point where the bottom of the pot is coming into view. The FAA recently reduced its estimate of Trust Fund revenues for FY2005 by nearly 25 percent – from $14.5 billion (projected in 2001) to $10.9 billion,[2] and the Air Traffic Organization (ATO) is projecting an $8.2 billion

[1] H.R. Conf. Rep. 91-1074, reprinted in 1970 U.S.C.C.A.N. 3101.
[2] *Next Steps for the Air Traffic Organization*, Statement of the Honorable Kenneth M. Mead Before the Committee on Transportation and Infrastructure, Subcommittee on Aviation, United States House of Representatives (April 14, 2005) p. 2 ("Mead Testimony").

cumulative gap between projected revenue and spending over the next five years.[3] Appropriately, the Trust Fund's balance and revenue projections are requiring a reexamination of spending priorities and calling into question the cost-effectiveness of expenditures and the benefits derived by various users of the National Airspace System (NAS). At the same time, the dire financial state of the U.S. airline industry is forcing a reassessment of the growing tax burden imposed on commercial aviation and the value we receive for our tax dollars.

The ATO Annual Report for 2004 sounds the alarm: "Revenue per flight is trending downwards in unprecedented ways."[4] One cause, of course, has been a sharp decline in fares, which has reduced revenue from the 7.5 percent ticket tax. In fact, FAA estimates that ticket tax revenues per aircraft decreased 33 percent in real terms from 2000 to 2003.[5] Of course, affordability of air service was one of the hoped-for benefits of deregulation and ticket tax revenues simply mirror what people are willing to pay for air travel. Ticket tax receipts have never been a good indicator of demand on the system. At the same time, what is often lost sight of is that non-commercial flights make up a large and growing proportion of NAS users but generate *de minimis* receipts – around two percent of Trust Fund revenue.[6] Overall, the excise taxes that make up the revenue stream for the Trust Fund are not keeping up with the growth in demand for ATC

[3] Statement of Gerald Dillingham, General Accounting Office, *National Airspace System: Progress and Ongoing Challenges for the Air Traffic Organization,* Testimony Before the Subcommittee on Aviation, Committee on Transportation and Infrastructure, House of Representatives (April 14, 2005), p.13 ("Dillingham Testimony").
[4] *Year One – Taking Flight: 2004 Annual Performance Report*, Federal Aviation Administration, Air Traffic Organization (March 2005), p. 23 ("ATO 2004 Annual Report").
[5] ATO 2004 Annual Report, p. 24
[6] This includes the excise tax on gasoline used for aviation purposes (AvGas), the excise tax on noncommercial use of jet fuel, and a nominal portion of ticket tax receipts.

services. Between FY 2003 and FY 2004, IFR operations increased by 5.5%, but Trust Fund revenue increased by only 3.95%, and revenue per IFR operation actually *decreased* by 2%.[7]

Administrator Blakey and ATO Chief Operating Officer Russ Chew have both recently called for "a revenue stream based both on our costs and on our actual units of production."[8] This has been over-simplified by some as a call for "user fees," and just as quickly opposed on that basis. It is important to keep in mind, however, that the *existing* Trust Fund was established by Congress to hold revenue generated "through the imposition . . . of airport and airway user charges" and that Trust Fund revenues were intended to be "raised and allocated according to the costs imposed by the respective system users."[9]

The question, then, isn't whether the Trust Fund should be funded by its users. Regardless of whether they are called "user charges," "user taxes," or "excise taxes" the fact remains that the system is *already* funded by its users – indeed, it is funded almost entirely by commercial aviation – a subset of its users. Rather, the question is whether the funding formula should be re-calculated or entirely reconceived to correspond more closely to the costs imposed by the respective system users. There are many competing theories on the best way to do this. While it is too early in the process to start debating

[7] ATO 2004 Annual Report, p. 21.
[8] Statement of Russ Chew, Chief Operating Officer, Air Traffic Organization, Federal Aviation Administration, on Transforming the FAA: A Review of the ATO, Before the Committee on Transportation and Infrastructure, Subcommittee on Aviation, United States House of Representatives (April 7, 2005) ("Chew Testimony").
[9] H.R. Rep. No. 91-601, reprinted in 1970 U.S.C.C.A.N. 3047.

the relative merits of one method over another, we believe that an approach that ties revenues to actual costs and assesses the burden proportionately can produce a funding mechanism that is simpler and more equitable, and a revenue stream that is able to keep pace with changes in the use of the aviation system.

II. Allocation of Trust Fund Expenditures

A. Funding for Air Traffic Management

The lion's share of appropriations from the Trust Fund – $7.9 billion in FY 2004 – goes to supporting and improving the air traffic control system, including maintenance of a nationwide infrastructure of more than 631 staffed air traffic facilities and nearly 41,000 systems such as radars and antennae.[10] Not surprisingly, the financial state of the Trust Fund has a direct bearing on the ability of the Air Traffic Organization (ATO) to carry out its mission:

> "The continued growth in cost of the air traffic control system at the same time that trust fund revenues are flattening and record high deficits are expected will put continued financial pressure on the ATO. All of the ATO's efforts to improve financial management, cost awareness, and management accountability will allow us to aggressively manage costs. However, even with an aggressive cost management program in place, we expect significant future gaps between FAA's annual costs and annual trust fund revenue."[11]

The cause of the predicament outlined above is not just a temporary shortfall in funds – it is rooted in the funding scheme itself. Because the excise taxes that go into the Trust Fund are unrelated to the cost of providing service to NAS users, it is virtually guaranteed that revenue will not be synchronized with operating expenses.

[10] ATO 2004 Annual Report p. 11.
[11] ATO 2004 Annual Report, p. 28.

1. The ATO Today

The challenge of maintaining the safe and efficient operation of the NAS while simultaneously investing in new technology and infrastructure necessary to meet future demands is nothing new – back in 1997, the National Civil Aviation Review Commission (NCARC) identified the urgent need to make significant changes in our aviation system:

> "The aviation system of the United States is at a critical crossroads . . . Unless the FAA and various aviation stakeholders – the Congress, the Executive Branch, and the aviation community – change the status quo, internal and external to the FAA, our nation's aviation system will succumb to gridlock. Delays will skyrocket while we reminisce about the 'reliable' flight schedules of the past. This current course will impair our domestic economy , reduce our standing in the global marketplace, and result in a long-term deterioration of aviation safety."[12]

The Commission called for "dramatic changes in the way that the air traffic system and airport development are managed and financed," and in partial response, Congress passed the reforms of AIR-21, which created a performance-based organization with greater flexibility as well as greater accountability. With Russ Chew's appointment as Chief Operating Officer in 2003 and the formal establishment of the ATO in February 2004, the FAA has taken important first steps towards averting the calamitous vision described above – but we know much more remains to be accomplished.

Unfortunately, time has not stood still in the half-dozen years it took to launch the ATO. Although the unforeseeable events of September 11, 2001 resulted in a brief decline in

[12] *Avoiding Aviation Gridlock and Reducing the Accident* Rate, Report of the President's National Civil Aviation Review Commission (December 1997) ("NCARC Report").

operations, the gridlock predicted by the Mineta Commission has advanced rapidly. The challenge described in 1997 still confronts us, with the difference today that the FAA must strive to meet the challenge in the face of unprecedented fiscal constraints, and service demands from a growing variety of other system users.

There is no doubt that the NAS will have to expand capacity and improve efficiency over the next decade to keep pace with the demand for air travel. Passenger enplanements last year were close to pre-September 11 levels, and the FAA is predicting that by the end of 2005 commercial aviation flights will have regained the peak levels of 2000.[13] Fourteen key airports – representing 23 percent of the total ATC operational workload – are experiencing unprecedented demand for air traffic services.[14] Growth in business aviation, spurred by models such as fractional ownership, has added significant flight operations at commercial and general aviation airports and in the surrounding airspace. A shift to smaller aircraft – regional jets as well as business jets – has increased both the number of operations and the complexity of air traffic management. Operations at en route centers actually surpassed the number handled in 2000.[15] Although these numbers are positive signs of a much-needed rebound in air travel, a less positive indicator of the return to pre-9/11 conditions is the steady increase in delays, which for the first few months of this year are also at or above year 2000 levels. "Aviation gridlock" was only briefly delayed by 9/11, and in the interim few measures have been taken to avoid it.

[13] ATO 2004 Annual Report, p.23.
[14] ATO 2004 Annual Report, p.23.
[15] Mead testimony. p.2.

The ATO has gotten off to a good start by focusing on finally establishing a true cost accounting system, streamlining functions, flattening hierarchy and developing new methods for evaluating performance, but the hard choices lie ahead. The ATO has inherited a long list of legacy systems with inscrutable acronyms, some of which have been in the pipeline for a decade and are still far from implementation or have failed to achieve their goals. Just sifting through these projects and determining which ones are still viable – and more importantly, would deliver benefits commensurate with their costs – is an overwhelming task. But that's not all – the ATO has also inherited a maintenance and repair backlog for the physical infrastructure that houses the ATC system. The existing physical structures – the air traffic towers, en route centers and terminal approach control centers – are on average 30 to 40 years old. They will require refurbishing, replacement and constructive consolidation in the near future, to the tune of $2.5 billion a year.[16] In addition, the FAA is confronting the overwhelming task of hiring and training thousands of air traffic controllers to replace the estimated 11,000 controllers due to retire in the next decade. Like Lewis Carroll's Red Queen, Russ and his team are finding that it takes all the running he can do just to keep in the same place. But as Russ has observed, that's not good enough: "Air traffic in this country is dynamic and the ATO must be able to adapt to future demands seamlessly and effectively without compromising safety."[17]

Just maintaining the safety and efficiency of our air traffic system at the current level of operations is not an option. The ATO will have to increase capacity of the system to

[16] Dillingham Testimony, p. 13.
[17] Chew Testimony.

accommodate an estimated 25 percent increase in the volume of air traffic in the next decade.[18] Moreover, changes in the way the NAS is used – such as increased use by non-scheduled operations and smaller jets – are placing very substantial and largely unanticipated new demands on the ATC system,[19] while new technologies, such as "micro-jets" or "very light jets," could even more dramatically increase the number of operations. In fact, the Joint Planning and Development Office is seeking to expand capacity by as much as 300% by 2015 to accommodate changes in aircraft size as well as the projected growth in demand.[20]

Today's system is still built around an outdated 1950s radar control architecture, which has been described as "ground-based radars tracking congested flyways and passing information from control center to control center on the ground throughout the flight of an aircraft."[21] This results in gross inefficiency, high maintenance and operational costs and inflexible systems that cannot easily respond to changes in use patterns. In order to meet future demands, it will not be enough to simply add more capacity to the old ground-based technology. The air traffic system must be completely redesigned; we can't afford to simply recreate the present system and repeat the mistakes of the past.

Some of the measures needed to accomplish this goal will be unpopular and even painful, and once again, the airlines can relate. The ATO has already begun implementing some long-needed changes, but will have to do more in the coming years to increase

[18] Federal Aviation Administration, *Aerospace Forecasts, Fiscal Years 2005-2016*, Table 36, X-37.
[19] ATO 2004 Annual Report p. 23.
[20] Joint Planning and Development Office, Next Generation Air Transportation System Integrated Plan December 2004), p. 8 ("JPDO Plan").
[21] JPDO Plan, p. 2.

productivity and bring labor costs in line with other sectors, consolidate en route centers, improve efficiency of tower operations, maximize use of all resources, and make hard choices about whether to continue investment in legacy systems that provide marginal benefit.

Operating costs to support the existing NAS have become an increasingly significant portion of the ATO's capital account, leaving less and less available to invest in the future. In fact, according to the Inspector General, FAA's "modernization projects" now consist predominantly of "keeping things running" [22] and deploying long-delayed systems that are outdated before they are brought on line. Forty-five percent ($4.4 billion) of FAA's planned funding for the next five years would go to sustaining the major ATC systems. [23] All told, there is not much left over to apply to development and deployment of new systems – a result that does not bode well for the future. As one of the experts assembled by GAO last year observed, "Who anywhere would have a capital investment plan that was predominantly about standing still?"[24]

According to a recent study by two researchers associated with the DOT Office of Inspector General, FAA invested $43.5 billion to modernize the NAS[25] over the past twenty years without *any* reduction in costs per operation.[26] As the ATO 2004 Annual Report acknowledges:

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[22] *See* Mead Testimony, p. 3.
[23] Dillingham Testimony, p. 11.
[24] GAO, National Airspace System: Experts Views on Improving the U.S. Air Traffic Control Modernization Program, April 2005, p. 18 ("Experts Report")
[25] Experts Report, p. 1.
[26] Arthur A. Shantz and Matthew Hampton, National Airspace System Capital Investments Have Not Reduced FAA Operating Costs, *presented at* Transportation Research Forum Panel, March 8, 2005, p. 1.

> Historically, capital projects were geared to introduce newer technology and more reliable service to customers. We did not invest systematically in internal productivity improvements and cost-savings initiatives. Up to now, the FAA has developed capital and operating budgets separately, with success defined as completing the capital programs. The result was often higher operating costs regardless of the benefits realized.[27]

Due in large part to this bifurcation between capital and operating budgets, NAS infrastructure modernization has actually resulted in *higher* operating costs.[28] In the absence of an ever-increasing amount of funds, operating costs will inevitably grow to the point where they swallow up the entire capital account.

2. The Future of the ATO

Although the ATO is to be congratulated on reducing unit costs and increasing productivity over the past year,[29] challenges abound. Moving forward, operating cost efficiency must be the criterion for new capital improvements; operations and capital budgets must be linked and a cost-based accounting system must be fully implemented and strengthened. As acknowledged by the ATO, it "must understand the cost of our services, in order to balance supply and demand in the short run and to know what steps are needed to meet customer demand in the long run."[30] New technology has the potential to "open up the sky to much greater and more efficient utilization of airspace,"[31] but only if investments are made rationally and with an eye to future reductions in operating costs.

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[27] ATO 2004 Annual Report, p. 28.
[28] Shantz and Hampton, p. 5.
[29] Overall, the unit cost (cost per IFR operation) decreased by $17 or 3.62%, while productivity of controllers increased by 7-10%. ATO 2004 Annual Report, p. 44.
[30] ATO 2004 Annual Report, p. 13.
[31] JPDO Plan, p. 2/

The structural problems inherent in the way the work of the ATO is funded is widely recognized, with recent reports issued and statements offered by many leading experts. Secretary Mineta himself recently harkened back to the recommendations of the commission he chaired, and issued a call to "open the dialogue" on the financing of the aviation system of tomorrow:

> Back in 1997, we concluded that FAA needed a more sustainable and more predictable funding stream and suggested separating it from the appropriations process. Today, I believe more than ever that the time has come to take those recommendations off the table and get to work on them.[32]

A stable funding mechanism which collects revenue from all users of the system in direct relation to costs imposed would allow the ATO to engage in realistic capital planning and respond more nimbly to changes in the use of the NAS.

The ATO cannot accomplish this on its own. Congress must give the ATO the tools it needs to complete its transformation into a more business-like organization that is responsive to customer needs. One bipartisan commission after another has called for "a stable, predictable source of revenue that can be leveraged for future improvements,"[33] and we agree with Secretary Mineta that it is time to get to work on those recommendations. We cannot solve the current dilemma by simply increasing the existing revenue stream – alternative funding mechanisms *must* be considered. The most obvious and widely discussed is revenue bonding, which should be fully explored as a source for capital investments. Bonding offers one possible funding stream that may

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[32] Speech of Secretary of Transportation Norman Y. Mineta, given at the FFA Forecast Conference, Washington, D.C. (March 17, 2005).
[33] The National Commission to Ensure a Strong Competitive Airline Industry, *Change, Challenge and Competition: A Report to the President and Congress* (August 1993), p. 2.

more closely match the modernization needs of the NAS by providing an infusion of capital to purchase and install equipment before it becomes obsolete, while bond-financed capital investments that result in greater efficiencies and expanded use of the NAS could pay back the investment over time. There are many details to be explored, but the concept is worthy of a close look and serious consideration.

B. Funding for Airport Improvements

In FY 2004, almost 30 percent of Trust Fund expenditures – nearly $3.4 billion – went to the Airport Improvement Program. This $3.4 billion accounts for about 25 percent of the total capital revenue stream available for airport infrastructure improvements, and helps airports fill the gap between perceived future needs and currently available capital. In theory, the users of the NAS, who pay the excise taxes that fund the Trust Fund and in turn the AIP, derive benefit from these infrastructure improvements in the form of increased capacity and reduced delay throughout the system. Unfortunately more and more AIP funds are set aside for programs that have only a remote effect on system capacity. By law, state apportionments, the noise set-aside, and programs for reliever and other general aviation airports claim over 36 percent of the funds available, and most of the rest is apportioned according to a complex formula that has little to do with the needs of the national system. Only a small percentage – just 3.8% in FY 2003 – is available to the FAA as discretionary funding to be awarded where it is most needed to address capacity or safety requirements.

Moreover, the commercial airlines and their customers who provide the bulk of Trust Fund revenues through ticket and waybill taxes do not reap the benefit of many of the investments funded through the AIP. More than a third of AIP grants – over $1 billion – go to airports without commercial service.[34] And many of the critical improvements at commercial airports are funded through passenger facility charges (PFCs) that are collected from airline passengers on top of the taxes and fees paid into the Trust Fund.

C. Administrative and Operating Costs

The Trust Fund currently supports a significant portion of the FAA's overall operating expenses. Although some amount of Trust Fund revenue has historically covered non-capital expenses, the amount appropriated for operations and FAA administrative expenses has increased to an average of $5 billion a year over the past five years, while general fund revenue has not kept pace with the increase in operating costs. Operating costs are even threatening to overtake FAA's Facilities and Equipment Account – traditionally considered the primary source of capital funding – which currently allocates only 57% of its $2.5 billion budget to developing and acquiring air traffic modernization projects.[35] And even less will be going to developing new technology in the future. To remain within its budget targets through 2009 FAA has to cut its capital investment plan funding, a strategy that is at odds with the well-established need to modernize and expand the system.[36]

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[34] ATO 2004 Annual Report, p. 23, based on information provided by the Aircraft Owners and Pilots Association.
[35] In FY 2005, 17% of the F&E budget was allocated to personnel and related equipment, 11% to mission support (support contracts), and 15% to FAA facilities. *See* Mead testimony, p. 17.
[36] Dillingham Testimony, p. 15.

The difference between Trust Fund revenue and FAA budgetary needs cannot continue to be made by shifting money from capital improvements to operating costs. General fund revenue is a key part of any funding formula for the FAA. "The general fund contribution recognizes the relative value of public benefit (as opposed to aviation community-specific benefit) derived from FAA services."[37] Sufficient general fund revenues must be provided to support programs that benefit the general public, whether ensuring the safety of aircraft or providing economic benefits to small communities that otherwise would not attract commercial air service.

The Trust Fund was established with the primary goal of providing a dedicated source of funds to expand and improve the system. While there has been near-continuous debate over the amount, if any, that could go to cover operating costs, it has always been the case that capital improvements were intended to take priority. "The Airport and Airway Trust Fund was designed to provide a dedicated source of user funding to pay for airport and airspace improvements. It should not serve as a general fund asset for the federal government."[38] We have reached a point where that priority is no longer reflected in appropriations from the Trust Fund.

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[37] ATO Annual Report p. 22.
[38] *Change, Challenge and Competition*, p. 8.

III. Equitable Allocation of Costs and Benefits

The concept behind the establishment of the original Trust Fund remains sound: that the users of the national aviation system, rather than the general taxpayer, "should properly pay for a greater share of the cost" of that system.[39] ATA's passenger and cargo members have always been willing to pay their fair share of those costs, but the excise taxes that provide the revenue for the Trust Fund no longer bear any relation to the cost of the system. Moreover, the burden of those taxes falls virtually exclusively on providers of commercial service, including ATA's member airlines. Scheduled operations accounted for only 66 percent of IFR departures last year, yet commercial airlines and their customers contributed 91 percent of Trust Fund revenues through ticket taxes, segment fees, cargo waybills, and the like. Taking into account accrued interest and passenger facility charges, which airlines pay directly to airports for infrastructure improvements, this contribution exceeds 100% of the costs imposed on the NAS. In contrast, business aviation, which currently uses somewhere between twenty and thirty percent of air traffic services, contributes only minimally to its support. Commercial airline operations are subsidizing a significant and growing portion of system users.

I want to be clear here; we are not talking about personal aviation, visual flight rule types of activity, but rather the fact that a Gulfstream IV looks a lot like a commercial-service 737 to an air traffic controller – it uses the same services and facilities – but its operator pays a mere fraction of the taxes and fees imposed on the airliner. In 2004 more than a quarter of IFR departures were by non-scheduled operations, and over two million of these operations involved jet aircraft that are in most relevant respects indistinguishable

[39] H.R. Rep. No. 91-601, reprinted in 1970 U.S.C.C.A.N. 3083.

from their counterparts in scheduled service. The assumption of the original drafters of the Trust Fund that "heavier and faster aircraft are generally responsible for much of the increased need of sophisticated control facilities and approach and landing facilities"[40] is certainly no longer the case. Scheduled commercial service is just one of a growing number of system users placing demand on the air traffic system and requiring airport capacity. In fact, one of the primary justifications for the work on the Next Generation Air Traffic System (NGATS) is the "increasingly diverse future marketplace demanding a broader range of air transportation services," including a shift to smaller aircraft.[41] This makes it imperative that the funding system for the next decade be designed to dynamically match cost drivers with revenue.

The drafters of the Trust Fund authorization recognized the need to revisit whether the original excise taxes assured "an equitable distribution of the tax burden among the various classes of persons using the airports and airways of the United States or otherwise deriving benefits from such airports and airways."[42] These principles should guide reauthorization of the Trust Fund. Whether revenue is generated through traditional excise taxes or new fees and charges, the burden must be proportional and allocated based on the actual costs imposed by each user or class of users, and not according to an arbitrary formula. In addition to being cost-based, any funding mechanism adopted must be simple, transparent and dynamic, so that the demands placed on the system by growth in any part of the sector will be immediately reflected in the revenue stream.

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[40] The House Ways and Means Committee cited this as a justification for the weight-based component of the aircraft registration tax. *See* 1970 U.S.C.C.A.N. 3093.
[41] JPDO Plan, p. 4.
[42] *See* Airport and Airway Revenue Act of 1970, P.L. 91-258, section 209.

Furthermore, Trust Fund revenue must be tied to the legitimate costs of the NAS. Again, in the words of the drafters of the original Trust Fund authorization: "Because this legislation relates primarily to the development of the national system, it proposes to levy only such user fees as are necessary to meet the Federal responsibility to expand and improve the national airport and airway system."[43] Today, approximately 85 percent of *all* FAA appropriations are drawn from the Trust Fund,[44] including $4.5 billion to cover FAA operations. Siphoning money from the Trust Fund to support aviation programs that do not contribute to the NAS is something we can ill-afford.

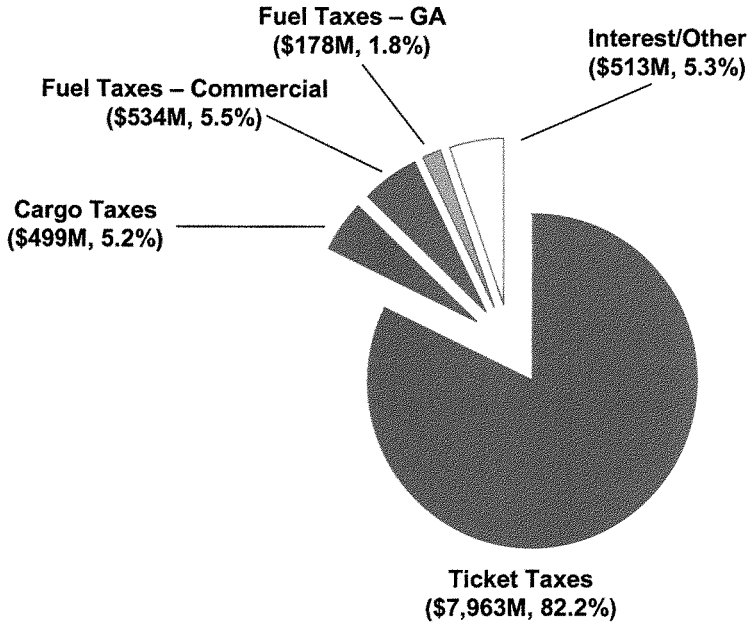
A healthy commercial aviation sector is critical to the U.S. economy. The present system for funding the Trust Fund and allocating money from it is out of sync with the reality of today's NAS. A cost-based funding mechanism that is simple, transparent, dynamic and equitable could do much to restore the health of U.S. commercial airlines by reducing their disproportionate tax burden while simultaneously providing the funds necessary to improve and expand the NAS. Congress should seize this opportunity to restore the Trust Fund to its origins, wherein users of our national airport and airway system should pay for its maintenance and improvement through an equitable, cost-based system.

[43] H.R. Conf. Rep. 91-1074, reprinted in 1970 U.S.C.C.A.N. 3101.
[44] ATO 2004 Annual Report, p. 21.

CHART #1

Trust Fund Revenues

Airport & Airway Trust Fund ($9,687M), Fiscal Year 2004

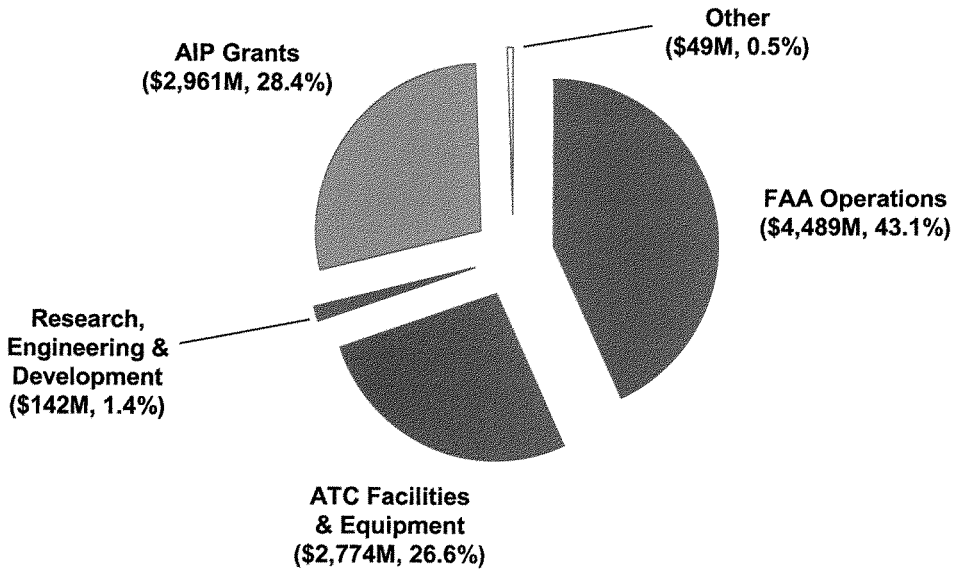


Source: Federal Aviation Administration

CHART #2

Trust Fund Expenditures

Airport & Airway Trust Fund ($10,415M), Fiscal 2004



Source: Federal Aviation Administration

Before the Committee on Transportation and Infrastructure
Subcommittee on Aviation
United States House of Representatives

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Perspectives on the Aviation Trust Fund and Financing the Federal Aviation Administration

Statement of
The Honorable Kenneth M. Mead
Inspector General
U.S. Department of Transportation

Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to testify on the state of the Aviation Trust Fund and financing the Federal Aviation Administration (FAA). This is one of the most important transportation issues currently facing the Congress, FAA, and the aviation community. The current FAA authorization—Vision 100—and the current ticket taxes expire in 2007.

Secretary Mineta and Administrator Blakey have taken important steps to begin the dialogue about the most appropriate way to finance FAA. Just last week, FAA hosted a conference on the status of the Trust Fund that sparked a good discussion of the problems. It set the stage for many of the issues that will be discussed today, but solutions are not as obvious as the problems.

Today, our testimony is going to address the following:

- The financial shape of FAA.
- Additional steps that FAA should take to control costs and determine current and future funding requirements
- Perspectives on financing options

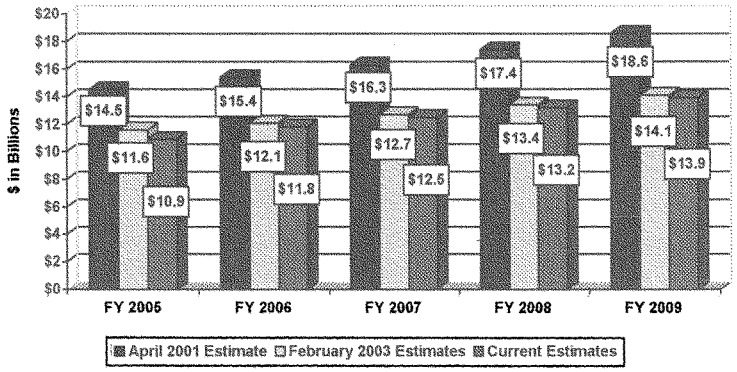
Financial Shape of FAA

In 1970, Congress authorized the creation of the Airport and Airway Trust Fund to provide a dedicated source for funding aviation programs. The Trust Fund collects a series of aviation excise taxes, which are used to fund a large portion of FAA's annual budget. Initially envisioned as the means to fund the infrastructure and modernization needs of the National Airspace System, the Trust Fund has also paid for large portions of FAA's operating budget, the Essential Air Service Program, and for one-time items such as security funding after the September 11th attacks.

The Trust Fund has provided FAA with a dedicated stream of revenue for many years; however, like the airlines, FAA is now facing a significantly changed financial landscape. In the past, increasing revenues into the Trust Fund and a large balance focused the debate on why funds were not being spent and how to "unlock" the Trust Fund. This is no longer the case.

While air traffic levels continue to show improvement from the sharp declines that began early in 2001, expected Aviation Trust Fund revenues have not materialized. In 2001, FAA estimated that Trust Fund revenues in 2005 would be about $14.5 billion, which would have exceeded FAA's Fiscal Year (FY) 2006 budget request. That estimate has now been reduced to $10.9 billion, a reduction of $3.6 billion or nearly 25 percent, of the 2001 estimate.

Figure 1. Estimated Trust Fund Revenues



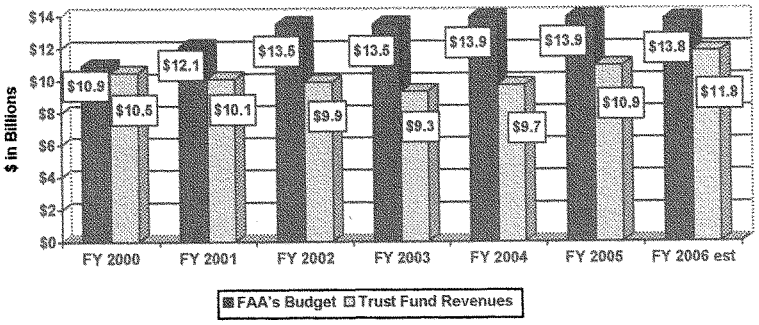
Those decreases can be attributed largely to reduced yields from the 7.5 percent ticket tax because of lower fares. The 7.5 percent ticket tax is the main revenue driver of the Trust Fund, accounting for about half of the tax revenues deposited into the Trust Fund each year. However, since 2000, the average air fare has dropped dramatically. For example, our analysis of Air Transportation Association data shows that in March 2000 the average cost of a ticket for a 1,000 mile flight was $149. In March 2005, it was nearly $118, a drop of over 20 percent.

Since FY 2000, revenues from the ticket tax have dropped from $5.1 billion to a low of $4.2 billion in FY 2003. With the enormous growth of low cost carriers and market pressure for continued low air fares, this phenomenon may reflect a long-term structural change within the industry.

A brief word about the segment tax, a potential funding source some have pointed to for bonding. It is a $3.20 charge on each segment of a passenger's flight and does not vary with the price of a ticket. In 2001, FAA estimated that this tax would generate about $2.5 billion in 2005, but the Agency now expects it to generate about $2 billion. By 2007, FAA expects the segment tax to generate over $2.3 billion.

While expected Trust Fund revenues have not materialized, FAA's budget has increased substantially. As shown in Figure 2, between FY 2000 and FY 2004 FAA's budget increased from $10.9 billion to $13.9 billion, an increase of nearly 28 percent. In FY 2006, FAA's budget is expected to exceed estimated Trust Fund revenues by $2.0 billion.

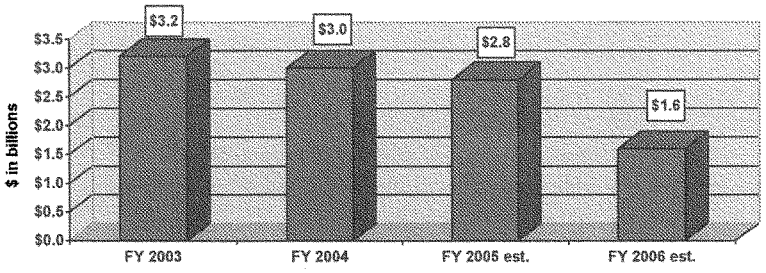
Figure 2: FAA's Budget vs. Trust Fund Revenues



Historically, the General Fund has been tapped to pay for some portion of FAA's budget. There are some exceptions, including FY 2000, when the Trust Fund paid for all of FAA's budget. For the last 10 years (FY 1996 to FY 2005), the General Fund contributed on average 21 percent of FAA's total budget.

As shown in Figure 3, General Fund contributions for FAA's budget have dropped from $3.2 billion in FY 2003 to $1.6 billion estimated for FY 2006, or 11 percent of FAA's total budget.

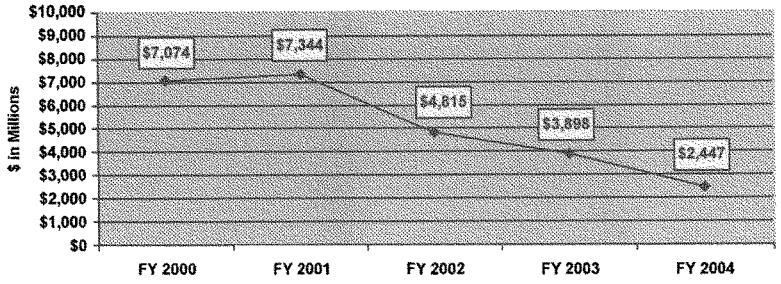
Figure 3: General Fund Contributions to FAA's Budget



Differences between FAA's budget and the contributions from the General Fund and Trust Fund have been made up by relying on the Trust Fund's uncommitted balance. For example, of FAA's $13.9 billion budget for FY 2004, Trust Fund taxes and interest collected that year provided $9.7 billon, the General Fund provided $3 billion, and the remaining $1.2 billion was provided by the

uncommitted balance. The following illustrates the decline in the Trust Fund's uncommitted balance.

Figure 4: Aviation Trust Fund Uncommitted Balance at the End of the Fiscal Year



FAA's budget has remained essentially flat at approximately $13.8 billion since FY 2004. However, there are significant differences in the distribution of FAA's budget among the Agency's various accounts. As shown in the Table 1, FAA is requesting increases above FY 2004 and FY 2005 levels for its operating budget but significant reductions for its capital account (Facilities and Equipment, or "F&E") and its Airport Improvement Program (AIP). With the budget staying flat, the effect is that the increased cost of FAA's operations is "crowding out" funds available for the Agency's capital and airport investments.

Table 1: FAA's FY 2006 Budget Request*
($ in billions)

	FY 2004 (Actual)	FY 2005 (Enacted)	Difference (05 to 04)	FY 2006 (Requested)	Difference (06 to 05)
Operations	$7.5	$7.7	$0.2	$8.2	$0.5
F&E	$2.9	$2.5	($0.4)	$2.4	($0.1)
AIP	$3.4	$3.5	$0.1	$3.0	($0.5)
RE&D	$0.1	$0.1	$0.0	$0.1	$0
TOTAL	**$13.9**	**$13.9**	**($0.1)**	**$13.8**	**($0.1)**

* Some figures do not add up due to rounding

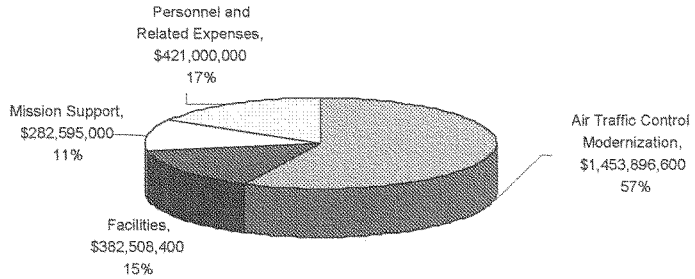
FAA is requesting about $2.4 billion for its capital account for 2006. This is about the same level as last year but significantly less than the nearly $3 billion FAA received in FY 2004.

As we noted in a hearing before this Subcommittee last month, the current funding level of FAA's capital account is not sustainable. This is a result of the combined effects of increased operations costs (salaries) and the fact that modernization

projects have suffered so much cost growth that there is little room for new initiatives. This explains why most of FAA's efforts now focus on keeping things running, or "infrastructure sustainment." And this is why there is so much discussion about how to finance new air traffic management initiatives.

Moreover, roughly 60 percent of the capital account goes specifically for acquisitions—the remaining 40 percent is for support contracts, facilities, and salaries. This is illustrated in Figure 5.

Figure 5: FAA's FY 2005 Facilities and Equipment Budget



Source: Analysis of FAA FY 2005 F&E Budget

At this Subcommittee's request, we reviewed 16 major acquisitions and found that 11 account for cost growth of $5.6 billion—more than 2 years' appropriations for the capital account. Additionally, 10 of these projects account for delays ranging from 2 to 12 years, and 2 projects have been deferred until at least 2008. There has been cost growth with major acquisitions since the establishment of the Air Traffic Organization (ATO), but the bulk of the cost growth represented by the $5.6 billion occurred before the establishment of the ATO. The growth is also a reflection of the ATO's efforts to re-baseline a number of projects, which identified costs that had been pent up for some time.

Before turning to options for financing FAA, I would like to talk about steps that FAA needs to take.

FAA Needs To Take Additional Steps To Control Costs and Determine Current and Future Requirements Before New Revenue Streams Are Explored

The Congress and the aviation community need assurances that FAA is doing all it can to control costs before decisions can be made about the adequacy of current funding levels and whether or not additional revenue is needed. There are four basic steps FAA needs to take—getting a handle on its cash flow requirements for existing projects in its capital account, controlling costs and improving the effectiveness of Agency efforts, finalizing the implementation of a cost accounting system, and determining funding requirements for future initiatives. Any business seeking an infusion of capital would take these steps. Moreover, these are preconditions for determining whether current funding sources will be sufficient or whether new revenue streams and authority are needed.

Determining FAA's Current Cash Flow Requirements for the Capital Account and Making Decisions on Projects That Have Been Delayed for Years. As noted earlier, projects already in the pipeline have been delayed by years and are substantially over FAA's estimates. FAA recognizes the need to obtain reliable information for its major acquisitions and is planning to update a number of program baselines. This will be important to establish the cash flow requirements on a yearly basis for the entire modernization portfolio.

Key decisions need to be made on projects like the Standard Terminal Automation Replacement System (STARS). For example, FAA revised estimates show that a "full STARS" solution (the replacement program of computers and controller workstations at terminal facilities) would cost over $2 billion. FAA has been studying its approach to terminal modernization since 2003 and is committed to assessing alternatives. A decision needs to be made on what technology is needed to complete terminal modernization based on time, cost, and capabilities.

FAA Must Take Additional Steps To Control Costs and Improve the Cost Effectiveness of Agency Efforts. FAA is taking important steps to control costs. The recent Flight Service Station decision has the potential to make significant savings—$1.7 billion over 10 years. We outlined a number of other things in a recent hearing before this Subcommittee that could save money. They include, but are not limited to, (1) controlling costs on support contracts valued at $2 billion and (2) taking proactive steps with the $2.1 billion En Route Automation Modernization (ERAM) project.

Getting a handle on support service contracts is a key area for savings. This is particularly the case for three large Indefinite Delivery contracts valued at over $2 billion that involve over 100 contractors. We have concerns over exactly how the contractors' work differs from work FAA employees do but at substantially higher costs to the Government. For example, one of the contractor's employees

on one task order is a retired FAA support staff manager who earned $109,000 just before retiring from FAA in 2003. This same person went to work for the contractor (within days of retirement) as a senior financial analyst, performing the same type of duties but at an annual rate charged by the contractor of over $206,000. The savings from greater control over these contracts could be substantial.

Also, FAA can reduce risk and potential for cost growth with the $2.1 billion ERAM effort. The purpose of ERAM is to replace the Host computers (the brain and central nervous system) for facilities that manage high-altitude traffic. The ERAM contract is currently a cost reimbursable agreement that places most of the risk with the Government. The early stages of this effort are within schedule and budget, but the heavy lifting of software development lies ahead.

Significant opportunities exist to control costs through the use of fixed price agreements for items not yet negotiated. FAA can also streamline software development and assess advantages of the state-of-the art computer capabilities to centralize computer processing that allows for sufficient redundancy.

At the recent Trust Fund Forum, a number of participants wanted to know what additional cost cutting measures could be taken by FAA and view cost control as an element in the debate about financing alternatives.

Implementing a Cost Accounting System and Getting a Labor Distribution System in Place. Progress is being made with developing a cost accounting system, particularly in the last 2 years. It is a critical tool for FAA because it has the potential to make significant contributions to assessing Agency cost centers and will help allocate costs among users. A cost accounting system includes a labor distribution system, which will help FAA manage its labor costs. FAA's cost accounting system has been delayed for years at significant taxpayer expense ($51 million), but the Agency has made the deployment of an effective cost accounting system a priority and plans to have a fully operational system in place by September 2006.

However, there are several hurdles that still need to be overcome. FAA must complete changes in the system to account for its recent organizational changes involving the ATO, begin assigning actual labor costs and other unassigned service costs to facilities and activities, and link performance measures to the cost accounting system. Addressing those issues is central for FAA to achieve the potential performance efficiencies and cost savings associated with an effective cost accounting system.

A reliable system to track labor costs is also a basic requirement for an effective cost accounting system. Labor distribution is the process of associating labor cost directly with activities and services by requiring employees to record their time

worked on specific activities. A labor distribution system represents an improvement because FAA can account for time spent by controllers managing traffic (on scope) and performing other tasks. This is critical given that over 73 percent of FAA's operating budget costs are made up of personnel compensation and benefits.

FAA is deploying a labor distribution reporting system for the ATO which, when fully deployed, will be used by about 35,000 employees. The system is running at over 100 terminal facilities (out of almost 300) and expects to have all terminal sites running by the end of June. FAA has also begun testing the system at en route facilities. FAA has committed to implement the labor distribution system and link the labor distribution system to the cost accounting system by December 2005.

Determining Funding Requirements for New Initiatives, What Capabilities Will Be Pursued, and When They Can Be Brought On Line. At last month's hearing on the ATO, there was considerable attention focused on the importance of the new Joint Program Planning and Development Office at FAA and what the new office can deliver. This new office is expected to coordinate research among diverse Federal agencies, including the National Aeronautics and Space Administration and the Department of Defense, with a focus on the 2025 timeframe. The office has published a plan, but FAA has not provided details on what capabilities will be pursued or how much they would cost to implement—this will be critical for determining the Agency's capital needs.

While the 2025 timeframe has merit, benchmarks for what can be done in 5- and 10-year intervals are also important. The other imperatives focus on determining what level of funding is actually required, how much other agencies will contribute, what specific capabilities will be pursued, and when they can be implemented. The Department committed to the Chairman that by the year's end, they would provide specifics on how much money is needed, when they will need it, and for what purposes.

Options and Alternatives for Financing FAA

Once FAA addresses the steps we just outlined, Congress and the Administration will be in a much better position to judge what FAA's financial requirements are and explore options. There are a number of options for financing FAA—none of them are painless.

Greater Reliance on the General Fund. As noted earlier, the General Fund has provided on average of about 21 percent of FAA budget over the last 10 years. Except for FY 2000, when the General Fund did not contribute anything, the contribution from the General Fund to FAA's budget has ranged from $1.1 billion (FY 2002) to almost $3.8 billion (FY 1998). Past studies and commissions have

recognized a General Fund contribution for FAA's safety oversight functions and Government use of the system, including the Department of Defense. Clearly, the role of the General Fund is an important element in the debate and was discussed at FAA's recent Trust Fund Forum. It is difficult to expect an increase above historical levels from the General Fund, given the competition for funds from other Federal programs and the current deficit environment. The debate would be better informed if a specific level of funding from the General Fund is identified for planning purposes as various alternatives are examined.

Reliance on Taxes. The primary source of revenue into the Trust Fund is the 7.5 percent ticket tax, but there are other taxes, including the $3.20 segment tax. The ticket and segment taxes combine for almost 70 percent of Trust Fund revenues. There is some controversy about the current system and whether the wide range of users are paying their equitable share of the services they receive. As was noted at FAA's Trust Fund Forum, the current excise taxes bear little resemblance to services various airspace users receive. For example, airlines contend that other airspace users are utilizing many of the same services they do but do not contribute their fair share. On the other hand, the General Aviation community (piston-powered aircraft) argues that they are only marginal users of a system designed primarily for the airlines and as such pay their fair share. The following provides information on the current taxes.

Table 2: Listing of Current Airport and Airway Trust Fund Taxes

Tax	Rate	Percentage of Total Tax Collections in FY 2004
Ticket Tax	7.5% on Airfares	49.7%
Segment Tax	$3.20 per Flight Segment	19.6%
Rural Airport Tax	7.5% on Airfares from Rural Airports	0.8%
Waybill Tax	6.25% on Price of Freight and Mail Transferred by Air	5.4%
GA and Jet Fuel	GA Fuel 19 3 cents/gallon Jet Fuel: 21.8 cents/gallon	1.9%
Commercial Jet Fuel	4.3 cents/gallon	5.8%
International Departures/Arrivals	$14.10 per international departure/arrival	14.4%
Alaska/Hawaii Tax	$7.00 per domestic departure/arrival to Alaska or Hawaii	0.8%
Frequent Flyer Tax	7.5% on proceeds of third party sales of frequent flyer miles	1.6%
Total		**100%**

Source: FAA

Given that FAA still has to establish its current and future funding requirements, it is difficult to determine the level of increase in revenue that would be needed, even if this was under consideration. Also, there is the issue of elasticity of demand—the airlines contend that they cannot pass on a tax increase to the flying public.

User Fees. Under this approach—also referred to as fee-for-service—fees collected from airspace users would replace most taxes. They have long been a favorite of economists, make sense conceptually, and were a core recommendation of the National Civil Aviation Review Commission (NCARC) report in 1997. Unlike the current system where the taxes paid by users bear only a limited relationship to the cost of the services they use, the fees charged under a defensible user fee system would be directly related to the cost of providing services.

However, before a defensible and equitable user fee system can be considered, FAA needs to complete its cost accounting system. This will allow FAA to determine what its costs are and allocate those costs to the various users of the airspace system.

Efforts to adopt user fees have met with stiff opposition from some quarters in the past, including the unsuccessful proposal in 1995 to spin off air traffic operations into an independent government corporation (U.S. Air Traffic Services Corporation, or USATS). In 1999, the Clinton Administration again proposed a shift from excise taxes to cost-based user fees, but that too was unsuccessful. These proposals were unsuccessful for a variety of reasons, including an intense debate surrounding who should pay what, the potential impact on fares, and FAA's inability at the time to allocate the costs of its system.

Today, we are again faced with a similar debate. However, in some ways the landscape has changed. First, FAA is facing a bleaker revenue forecast. Second, FAA is nearing completion of its cost accounting system. However, the contentious issues of who should pay what and whether each stakeholder is paying its fair share remain central unresolved matters. These issues are important given the diverse mix of users in the National Airspace System that include general aviation, high-end general aviation or business aircraft, and regional jets, in addition to cargo and other commercial carriers. User fees will likely generate winners and losers—i.e., some users may pay more than they currently do and some may pay less.

The most common user fee constructs are based on a combination of the weight of the aircraft and the distance flown. Weight and distance fees are used by more than 100 countries. Although a weight-and-distance charge is direct, and probably

more cost-related than an excise tax, it too is less than a perfect measure of a user's cost to the system. While distance is a measure of cost to the system, an aircraft's weight does not materially affect the costs of providing Air Traffic Control services but instead is primarily a surrogate for that aircraft operator's presumed ability to pay.

Despite the difficulties, a positive feature of an equitable and defensible user fee system is that it should provide powerful incentives to control costs in an effort to contain increases to user fees, provided that an appropriate oversight mechanism, other than FAA, is developed. This should also translate into greater user involvement in investment decisions.

An option for formalizing this oversight mechanism is through the creation of a board that would set user fees and adjust them upward or downward over time. The NCARC report proposed a "public interest board" made up of Presidential appointees with at least three members knowledgeable in aviation but none with any financial stake in the industry. Another alternative, which is not mutually exclusive, is a "stakeholder board," like the one currently used by Nav Canada, with representation from key aviation segments (i.e., commercial aviation, general aviation, unions). In any case, decisions would need to be made regarding the board's authority beyond the setting of rates and the extent of its duties and responsibilities, including the preparation of business and financial plans.

Bonding/Borrowing Authority

Another funding mechanism that is being discussed is the question of bonding or borrowing. This is not a new idea. In 1997, the NCARC report recommended that services related to the air traffic system be placed in a Performance Based Organization and given authority for long-term borrowing from the U.S. Treasury or from private capital markets as part of a shift to user fees. Bonding/Borrowing was a major topic at FAA's recent Trust Fund Forum.

The rationale behind allowing FAA (or some entity on its behalf) to sell bonds is to provide it with a large infusion of funds for capital projects, including air traffic control technologies. The bonds would need to be backed by a well-defined, predictable source of revenue. There are several important preconditions to consider—FAA needs to finalize its cost accounting system, demonstrate its ability to control costs, and determine how much capital is needed, when it is needed, and for what purpose.

Granting FAA any type of bonding or borrowing authority would require legislative changes, consideration of complex budgetary scoring issues, and the impact on the Federal deficit. Equally important is the fact that certain bonding

models do nothing to ensure that the entity making the investment operates cost effectively or that the acquisition funded by the investment performs as anticipated. A model that does not provide powerful incentives to invest wisely and control costs could result in a substantial infusion of capital but do little to ensure that the acquisition performs as expected and is delivered approximately on budget and on schedule.

Bonding Construct With Limited or No Issuer Accountability. Several years ago a proposal was set forth for Amtrak to issue bonds in an effort to raise funds for Intercity Passenger Rail. Under this construct, bonds are sold in the capital markets with a portion of the funds set aside to repay the principal upon maturity. Rather than cash, investors are provided with a tax credit to generate the return that *is guaranteed* as these bonds either have or are perceived to have the full faith and credit of the United States. A variation of this model would isolate a portion of an existing tax and "securitize" it, thereby providing a large inflow of funds to be paid off over a number of years from the dedicated source.

This is essentially "sovereign debt" and per se, requires no accountability on behalf of the issuer since the repayment is guaranteed. As such, there is no linkage between the bond instrument and the performance of an acquisition. The investor receives a specified return regardless of whether the investment performs or is delivered on time and on budget, and no discipline is imposed on the issuer to control costs. The goal here is not to simply provide more money, but to ensure that funds are used wisely to provide capital for the next generation air traffic control system.

Bonding Construct with Issuer Accountability. Another form of bonding authority is more akin to bonds issued in the private sector or by municipalities. These bonds are issued in the public markets without the full faith and credit of the United States. The borrowing entity needs to operate in a business-like manner so that investors/Wall Street are able to analyze the volatility of the revenue stream (which is the ultimate source of repayment), the associated costs, and the financial plan as a whole.

This type of borrowing authority is usually considered in conjunction with a financing system that charges cost-based user fees and is consistent with the NCARC recommendation. These fees provide a bondable stream of revenues and the flexibility to price those fees to cover costs. Under this framework, and assuming the existence of an oversight board aside from the issuer, there are powerful incentives from users to control costs and deliver systems on time as this will ultimately keep the fees that users pay from increasing.

There is also the oversight of the public markets in scrutinizing the business plan supporting the debt issuance since the return is not guaranteed by the full faith and credit of the United States. Further, if the capital investment does not perform, investors will require that the issuer increase its interest rates the next time it goes to market, which in turn will increase the issuer's costs resulting in pressure to increase fees to users. Therefore, this construct would also encourage improved strategic planning as users will demand that capital expenditure decisions are based on real needs and a rational cost-benefit tradeoff.

Regardless of what approach is used, it is critical that: (1) there is a clear understanding of what investment the FAA would be borrowing money for (i.e. long-term investments in order to meet future demand); (2) it is not simply a short-sighted vehicle to put off increased fees or taxes in the near term and; (3) accountability and discipline is established to ensure cost control and efficient, on-schedule implementation of capital investments.

Congestion Pricing Must Be Joined With the Debate

Finally, the debate about FAA financing needs to joined with the issue of auction/congestion pricing at airports. The FAA is now soliciting comments on whether to continue the administrative controls at Chicago O'Hare for another three years—a regulatory approach that does not accommodate demand and can stifle competition. FAA is now funding research on auctions for landing rights for airports such as LaGuardia. Airports are also making the case for congestion pricing more broadly. We think this debate needs to be joined with the debate taking shape on financing FAA.

Aviation congestion is very clearly an issue that affects the national air traffic network as a whole, and it ought to be addressed at a national level. For example, recently a 10-minute delay for 15 jets approaching Newark affected 250 aircraft throughout the system, some as far west as Minneapolis.

Some difficult questions and policy issues have to be worked through. First and foremost is whether or not peak-hour pricing should be authorized. If so, a number of other policy questions will need to be addressed: Who sets the fees? Who gets the funds? The FAA? The airports? Some combination? What will the funds be used for? How will this effect General Aviation and commuter air traffic, and what will the impact be on service to smaller communities?

Mr. Chairman that concludes my statement. I would be happy to answer any questions that you or other members of the Subcommittee might have.

Congresswoman Juanita Millender-McDonald
Statement at Subcommittee on Aviation
Hearing on
Financial Condition of the Aviation Trust Fund: Are Reforms Needed?
Wednesday, May 4, 2005
2167 Rayburn House Office Building-10:00 A.M.

Mr. Chairman, thank you and Ranking Member Costello for holding this very important hearing.

How we fund our aviation system is of vital importance to how our entire transportation infrastructure operates and interacts with our population and the goods we move. One mode can not be under funded or it will through off the balance and effectiveness of our entire transportation system.

There have been fundamental shifts in the airline industry since 9/11. We have seen resources used for security and we have seen the market trend shift to smaller airlines.

The emergence of the regional, or low cost, carriers are bringing ticket prices down. While

this is good news for consumers, it is proving to be problematic for the future health of our infrastructure. Currently, a large portion of the aviation trust fund receives funding from the 7.5% charge on the total cost of a ticket. The lower ticket prices go, the less money goes into the aviation trust fund.

If prices continue to drop, we will eventually be faced with the difficult decision of either raising taxes or cutting spending.

I am looking forward to hearing from today's witnesses as we begin to address these long term funding issues.

I look forward to hearing from today's witnesses.

Thank you Mr. Chairman.

OPENING STATEMENT OF
THE HONORABLE JAMES L. OBERSTAR
AVIATION SUBCOMMITTEE
FINANCIAL CONDITION OF THE TRUST FUND: ARE REFORMS NEEDED?
MAY 4TH, 2005

I want to thank Chairman Mica and Ranking Member Costello for calling today's hearing on the financial condition of the Aviation Trust Fund, and possible alternative mechanisms for financing the future needs of the aviation system.

Mr. Chairman, while today we will hear varying opinions about the future of the Trust Fund, there is no disagreement that the Trust Fund's uncommitted balance has declined over the last few years. At the end of fiscal year 2000 the Trust Fund's uncommitted balance was a little more than $7 billion. At the end of fiscal year 2004 the Trust Fund's uncommitted balance was roughly $2.45 billion. As the Inspector General will testify today, Trust Fund revenue estimates for the last few years have been overly optimistic. The shortfall between projected revenues and actual revenues have been made up from the Trust Fund's uncommitted balance. For example, for fiscal year 2004, the actual receipts plus interest credited to the Trust Fund were almost $1.3 billion or 12% less than projected.

Some major questions before this Subcommittee today are – *are the FAA's revenue projections reliable?; Can we rely on these forecasts in determining funding levels for reauthorization?* To its credit, FAA has recognized that there are legitimate questions

about its forecasts, and FAA has initiated an independent review of FAA's aviation activity and revenue forecasting methodologies.

The downturn in passenger travel associated with the September 11th terrorist attacks clearly depressed Trust Fund revenues. There are also indications that underlying structural changes within the airline industry are affecting Trust Fund revenues, as well as the FAA's ability to forecast those revenues. For example, it has been widely suggested that the growth of low-cost carriers and corresponding fare reductions by legacy carriers have driven down passenger ticket tax returns that account for roughly 50% of annual Trust Fund revenue.

The FAA is currently predicting that Trust Fund revenue will increase over the next few years. The FAA's most recent estimate predicts that receipts and interest into the Trust Fund will increase 13.4% between fiscal year 2004 and fiscal year 2005. At this hearing we will want to learn FAA's basis for predicting this large increase.

Even with this large increase, FAA believes that revenues over the next few years will be less than was forecast when Vision 100 was enacted in 2003. The FAA is now predicting that $1.8 billion less will come into the Trust Fund over the next three fiscal years compared to what the FAA had estimated prior to Vision 100. Of course, actual revenues could be even less. The Government Accountability Office

(GAO) will testify that if revenues are 10% less than now projected, under current law, the Trust Fund's uncommitted balance would reach zero by 2007. If traffic is less than expected, or fares drop dramatically, or both, we will need to consider measures to address the shortfall which could include cutting the FAA's programs, raising taxes, or obtaining a larger general fund contribution.

Regarding the possibility of cutting the FAA's programs, last month the Inspector General testified before this Subcommittee that the "current budget level of the FAA's capital account is not sustainable." We clearly cannot continue to cut the FAA's capital budget and still technologically "transform" the national airspace system for the 21st Century.

Regarding the general fund contribution, I still strongly support the mechanisms Congress enacted in AIR-21, particularly the guaranteed funding provisions and the Trust Fund and general fund contribution formula. The FAA's programs should be fully funded at their authorized levels and if Trust Fund revenues fall short the general fund should contribute whatever it takes to meet the authorized levels. Moreover, hundreds of millions of dollars were spent from the Trust Fund after September 11th on aviation security measures that are now funded by the general fund through the Department of Homeland Security. That aviation security spending was national security spending, and I believe that a larger general fund contribution

may now be warranted as a reimbursement for security funding that was spent from the Trust Fund.

Mr. Chairman, some have suggested that we need sweeping reform of the current aviation tax system, such as the wholesale adoption of a cost-based user fee. While I am open to all ideas, I think the idea of switching to a user fee system raises more questions than answers. Here are just a few issues that I will raise right now –

- First, I do not understand how a user fee will generate more revenue than the current system unless the aviation community in the aggregate would pay more than it does now. To raise more revenue, someone will have to pay more.

- Second, it has been argued that cost-based user fees will lead the FAA to be more efficient in providing services. At first blush, this sounds somewhat theoretical to me. I would like to see some detailed explanations and evidence in the coming months regarding how precisely user fees alone will drive down FAA's costs.

- Third, a user fee system contemplates that the major system users, principally the airlines, will be saddled with the new fees. In return, airlines will expect to

play a greater role in setting the FAA's policies, and in deciding how much and what the FAA will spend its money on.

Additionally, some have suggested that Congress ought to consider alternative financing mechanisms such as bonding. Before Congress considers bonding authority, I think that the FAA should explain precisely what it would purchase with such authority. Further, we should anticipate that the Office of Management and Budget (OMB) and the Congressional Budget Office (CBO) will raise issues regarding how bonding authority will be scored against the discretionary budget.

Thank you once again, Mr. Chairman, for holding this hearing. I look forward to hearing from our witnesses.

Statement of David Z. Plavin
President, Airports Council International – North America
On Behalf Of:
The American Association of Airport Executives/Airports Council International – North America
House Aviation Subcommittee
Financial Condition of the Aviation Trust Fund: Are Reforms Needed?
May 4, 2005

Chairman Mica, Ranking Member Costello, thank you for the invitation to appear before the subcommittee today to offer the views of America's airports on the future of the Airport and Airway Trust Fund. I am testifying today on behalf of the American Association of Airport Executives (AAAE), Airports Council International–North America (ACI-NA), and the Airport Legislative Alliance, our joint legislative advocacy organization. AAAE represents the men and women who manage primary, commercial service, reliever, and general aviation airports. ACI-NA represents local, regional and state governing bodies that own and operate commercial airports in the United States, and Canada.

For the airport community, the importance of ensuring the financial stability of the Airport and Airway Trust Fund cannot be overstated. As you know, the Airport Improvement Program, which has proven enormously successful in building critical airport infrastructure and is one of the key methods by which airports fund capital development, is supported entirely by the Trust Fund. The FAA's Facilities and Equipment (F&E) budget, which includes funding for air traffic control modernization efforts and many important projects to increase capacity at airports, is also funded by the Trust Fund as are research, engineering, and development programs. Like AIP, these programs are critical to meeting the safety and capacity demands of the future.

Long-Term Solutions Needed to Prepare Aviation System for Future Demand

With both the user taxes that support the Trust Fund and the current authorization for Federal Aviation Administration programs set to expire at the end of fiscal year 2007, now is absolutely the right time to start the discussion on the long-term future of the Trust Fund and how we finance the nation's air transportation system. It is no surprise that this subcommittee and the Transportation and Infrastructure Committee are taking a lead role in this effort. After all, you were instrumental in shaping and passing AIR-21 and its successor legislation, VISION-100. Thanks to your leadership, federal investment in airport development has increased in recent years, enabling airports to make billions of dollars in much needed investments for runway, taxiway and apron construction and rehabilitation; airfield lighting; airfield signage; airfield drainage; land acquisition; planning studies; environmental studies; safety area improvements; airport layout plans; and airport security improvements.

Still much more needs to be done to keep pace with current demand and to prepare for the one billion passengers the FAA says will be traveling annually within the system by 2015. Looking forward, we must build on the successes of AIR-21 and VISION-100 by ensuring that adequate resources flow into the Trust Fund and that those funds, in turn, are used as promised for capital improvements based on system needs. Additionally, we must maintain the balance between Trust Fund revenue and general fund contributions to meet the diversity of FAA obligations. Nowhere is this more important than with supporting air traffic control operations, given the vital role that FAA's controllers play for our nation – both in support of commercial aviation and the military – and in light of the many benefits that each American, even those who never use the

system, derives from its safe and efficient operation. Today, it is clearer than it ever has been that aviation is not just a convenience, but a necessity that protects the lives and fortunes of all Americans.

Notwithstanding these principles, it is evident that today's aviation demands are not adequately supported by Trust Fund revenue and the money that the Administration is budgeting from the general fund. Accordingly, airports support Secretary Mineta's call for a thorough review of system needs and the financing tools necessary to meet those obligations. Airports believe that any such review must include a discussion of the roles and responsibilities of government, air carriers, general aviation and airports, as well as the means by which to finance the various obligations that support the industry. We note that airports today have stepped up to help address system challenges, often financing needs traditionally borne by the FAA such as hiring environmental consultants, financing technology upgrades and replacing air traffic control towers. Undoubtedly, this will make the next reauthorization discussions extremely challenging.

Airport operators face a bewildering array of outdated economic regulations that raise the cost of doing business, particularly in planning and building new capacity. Other regulations prescribe in great detail how we may raise funds and what we may and may not do with them. These bureaucratic dictates create an enormous cost of compliance both at the airport level and with FAA staffing levels. Airports support regulations that protect the safety of the system and the integrity of the market-based aviation system, including protections against unjust discrimination and illegal revenue diversion. But bureaucratic holdovers such as competition plans need to go. The results are higher cost to airports, airlines, and passengers, and a reduced ability to serve the industry responsively. Establishing the proper regulatory and statutory framework can unleash innovation and save valuable resources.

Some airports may even be willing to consider a broader set of options. These might include the possibility of foregoing participation in the AIP program in exchange for eliminating the artificial constraints imposed by outdated, burdensome, and counterproductive rules and regulations that make it impossible to operate in a businesslike fashion. In addition, providing unfettered local authority for the Passenger Facility Charge (PFC) program would promote better local solutions and provide more resources to the airports that rely on AIP as their sole, or near sole, source of capital development funding.

Airports have the capability to help the FAA to deploy much needed infrastructure. And, we have a number of other ideas we are eager to discuss, including proposed changes to the federal rules governing airport bonds, which are the source of the majority of overall airport capital development resources.

In Short-Term, Congress Must Reject Massive Cuts to AIP, ATC Modernization Efforts

While we look forward to a discussion of future financing options, our more immediate concern is funding for FAA capital programs in fiscal year 2006. As you know, the Administration's proposed budget calls for only $3.0 billion in funding for AIP, a nearly $500 million reduction from the FY 2005 enacted level and a $600 million reduction from the amount authorized in FY 2006. The proposed cut to AIP is one of the five biggest in all of the federal government. The F&E account also has been targeted for a major reduction in funding for the second year in a row.

The Administration's proposed cut to AIP defies logic given the program's success as verified by the Office of Management and Budget and in light of the FAA's own forecasts, which show traffic levels increasing dramatically in the years ahead. According to data released by the FAA recently as part of its annual forecast conference, U.S. commercial air carriers are expected to carry more than one billion passengers annually by 2015, up from less than 700 million passengers in 2004. Cargo and general aviation activity are also projected to grow significantly.

With an additional 300 million people expected to be added to our already crowded aviation system over the next decade, it is critical that we make the necessary investments in airport infrastructure today. Runways, which can increase capacity at an airport by 30 to 60 percent according to the FAA, can take a decade or longer to plan and build. Other infrastructure projects similarly can take years to develop. Thus, the effect of funding reductions now may not be fully felt until years down the road, just as those hundreds of millions of additional travelers crowd the aviation system.

In a June 2004 report entitled "Capacity Needs in the National Airspace System," the FAA looked at the future of airport capacity at 35 of the busiest airports in the country as well as nearly 300 other commercial service airports in more than 200 metropolitan areas. Not surprisingly, the study found that there are a handful of airports in desperate need of additional capacity now and many more that will need capacity in the relatively near future. One of the key conclusions of the report was that "[t]he predominant trend over the next two decades largely will be the expansion of existing airports to meet forecast demand. Because of the long lead times necessary to bring large complex runway projects on line, current improvement plans must move forward to keep pace with demand forecast for 2013. If the planned improvements do not occur for any reason, the number of airports experiencing capacity shortages will grow sharply."

Simply put, if we don't plan, finance, and start building these projects today, our economy, the industry, and travelers will suffer in the years ahead. Instead of helping to meet this demand, the FAA will be attempting to manage airside, terminal and ground congestion at almost every large airport in the nation.

Beyond necessary capacity enhancements, a $500 million to $600 million cut to AIP could seriously affect the ability of airports – particularly smaller facilities – to tackle much needed safety and security upgrades and other pressing projects. AIP cuts disproportionately impact smaller airports that do not have ready access to capital markets or other resources for key infrastructure projects. For a number of airports, AIP is the life blood for capital projects that allows them to keep their facilities operational and up to FAA standards.

The only possible explanation for a proposed cut of this size is budget gamesmanship. Senate Transportation Appropriations Chairman Kit Bond (R-MO) hit the nail on the head with the assessment he offered during a recent hearing on the DOT budget:

> **"While I respect and support the efforts of the Administration to reduce the deficit, I do not believe that it is appropriate to balance the Federal books on the back of critical transportation infrastructure programs. For example, the Airport Improvement Program is slated for one of the largest reductions in the entire fiscal year 2006 budget request, despite a proven track record that enhances airport safety, capacity, and security. After the program received high marks in the OMB PART process, I am at a loss to understand why this program remains in the sights of the budget gnomes."**

Mr. Chairman, we have all invested too much of our time and resources to turn back the clock to the days before the passage of AIR-21 and VISION-100. As you recall, AIP and other FAA capital programs were routinely held captive in those days to the artificial constraints of the federal budget process and were dramatically under-funded despite a steady stream of user paid revenues and despite promises made to those system users that their taxes would be used for investments in the aviation system. The disastrous summer of 2000 – when one in four flights were delayed or cancelled – is part of the unfortunate legacy of that period. Today, we have again reached the passenger levels of that year, and aircraft scheduled for the summer of 2005 have already surpassed the numbers of flights scheduled in 2000. We set the stage for repeating those mistakes for the foreseeable future unless we act now to invest in the nation's airports and aviation system.

Why has this happened?

Over the last decade, more and more of the Trust Fund has been depleted by a regular and systematic addition of operations funding despite the original intent of the fund, which was to support airport and airways investments. As the revenues in the fund have not grown as projected, the squeezing out of investment funding has accelerated. The effect becomes even more dramatic as the Administration proposes to cut $1.6 billion from the general fund contribution to FAA operations funding, reducing the level of FAA's general fund support from an FY 2005 level of 19.4 percent to 8 percent in FY 2006. The missing general fund support is made up by draining the unobligated balance of the Trust Fund to nearly zero, a risky proposition.

The Case for Fully Funding AIP at $3.6 Billion

While we firmly believe that the debate on AIP and other FAA capital programs this year has more to do with macro budget politics than the merits of individual programs, we are compelled to respond to some of the arguments the Administration has presented in trying to justify its proposed cuts to AIP.

FAA's NPIAS Report: First, Administration officials have suggested that an AIP funding level of only $3 billion is acceptable in light of decreased capital needs. First, it is important to remember that the National Plan of Integrated Airport Systems accounts for only a select portion of AIP-eligible projects and does not account for any projects funded by PFCs nor the majority of airport projects funded by revenue bonds. For example, it does not account for the close to $1 billion airport tunnel and people mover program which is long overdue to enhance inter-terminal access for passengers underway at Dulles International Airport.

The NPIAS, in fact, measures only AIP-eligible projects for which airports have not designated a funding source and that the FAA (not the airport) deems warranted and believes will be built between 2005 and 2009. For this cycle, the NPIAS estimated that $39.5 billion in AIP-eligible infrastructure development would be needed to meet all of the needs of civil aviation, a figure that is nearly 15 percent lower than the preceding report, issued in 2002. In general, AIP-eligible capital project estimates for large hub airports decreased while estimates at smaller airports increased when compared to the previous report. While many airports certainly postponed some projects after 2001 and 2002 – especially terminal and ground-side projects as airports prudently

waited to see how the new security mandates would work out – airport development has since taken off as frequent visitors to airports know.

ACI-NA is in the process of finalizing its own periodic airport capital development need assessment. Based on in-depth surveys with nearly 80 of our members representing 77 percent of total U.S. passenger activity, our preliminary work shows that the $39.5 billion figure used by the FAA in the NPIAS represents a figure that is at least 25 percent below actual capital needs. I would hasten to add that ACI-NA has conducted similar surveys since 1990 and that our work has repeatedly been cited as an important source by the Government Accountability Office (GAO) and the Department of Transportation Inspector General.

Part of the difference between FAA's findings and those of ACI-NA is timing. The FAA's NPIAS data was compiled in November of 2003, meaning that it was actually collected well before that time – right in the midst of the post 9/11 low point. ACI-NA launched our capital needs survey in November of 2004 and the majority of the data we have received was submitted in the first three months of this year. We appreciate the FAA's willingness to sit down with us and attempt to reconcile our different estimates of AIP-eligible projects. We will use the information we learn from those meetings to help with the estimate of all capital needs. We have also met with the GAO on our estimates and look forward to their helping us reconcile the different estimates.

Given the dramatic changes in the aviation industry over the past year to 18 months, it is not surprising that our findings would be different than those of the FAA. Airports, which had initially put some projects on the back burner given the uncertainties that followed the 2001 downturn, have begun more aggressive planning in the face of anticipated increases in demand as verified by FAA forecasts. Some airports, such as Washington Dulles airport with the arrival of Independence Air, have seen dramatic increases in capital needs over that time period that are not accounted for in the FAA's NPIAS work.

It is also worth noting that construction costs in general have increased dramatically over that time period and are likely to continue climbing. These increases are documented in the *Engineering News Record's* costs indexes, which show in 2004 a 7.8 percent increase in construction costs, a 9.7 percent increase in building costs, and a 20.3 percent increase in materials costs. In every area of the country, the cost of steel, land, fuel, and other materials has risen substantially, a fact that adds to the discrepancy since the FAA NPIAS does not account for project cost inflation.

Regardless of what the final estimates are for NPIAS and overall capital needs, it is evident that cumulative AIP funding over that same period will not even pay for those $39.5 billion in NPIAS-identified needs, even under the most optimistic of assumptions. A program funding level of $4 billion over those years would still leave a funding gap of nearly $20 billion.

While some airports do have access to other sources of capital such as airport bonds in addition to AIP funds to help "fill" that gap, turning increasingly to those options does come at a cost to travelers and to our airline partners, who can least afford it now given their tenuous financial footing. It is also important to note that the $39.5 billion figure does not include a host of non-AIP eligible items such as parking, hangars, air cargo buildings, and the revenue producing portion of passenger terminal buildings that airports must find a way to pay for as well.

"Untapped PFCs": FAA has also attempted to justify its reduction in AIP funding, in part, on the assertion that there exists a substantial untapped PFC capacity available at airports. This is among the most creative and flawed arguments to justify a budget request in many years. The FAA's primary evidence of this assertion is that one airport system operating a large hub airport (Houston) does not have a PFC and that an additional handful of airports have not yet received approval for the maximum allowable PFC charge level of $4.50. Therefore, the FAA argues, that this financial capacity is "available" to airport needs. This assertion is flawed in a number of ways.

First, their estimate does not include those PFC applications that are pending at the FAA. Those applications should be processed expeditiously so airports can proceed with their needed investments. Since the number was calculated, additional airports have applied for the $4.50 PFC. In fact, only one airport system that operates large hub airports doesn't have a PFC (Houston).

Second, the FAA does not discount the monies that a local airport will forego if they raise their PFC. When an airport moves from no PFC to $3.00, that airport loses 50 percent of its AIP entitlement. Once an airport moves from a $3.00 PFC to $4.50, the airport loses 75 percent of its original AIP entitlement.

Third, PFC revenues are local and are not portable. Airports are not permitted nor do they have the incentive to spend locally-raised PFC revenues at another airport operated by a different authority. Kansas City, Missouri, which has not increased its PFC from $3.00 to $4.50, for example, cannot increase its PFC level and give the money to Chicago to pay for the needed improvements to the airfield at O'Hare International.

Fourth and most critical, a decision by an airport operator on PFCs and other rates and charges are and must remain local decisions, determined by the airport operator together with its community of airlines. This consultation approach is exactly what is encouraged in the FAA's own process for approving PFCs. It is in no way appropriate to view them as federal funds to offset reductions in federal funding.

All Capacity Needs Can Be Met in FY 2006: Finally, some Administration officials contend that the $3 billion level proposed by the President will allow FAA to fund all capacity related programs in FY 2006. While it is clearly not possible that cuts of more than half a billion dollars will have no effect on airport capacity projects in FY 2006, the bigger question perhaps is what the cut might mean in future years if it is allowed to stand.

As every member of this subcommittee is aware, funding the program at only $3 billion in FY 2006 will effectively make that figure the program baseline and render it extremely difficult to gain funding beyond that level in future years. With the authorized program levels at $3.6 billion and $3.7 billion respectively for FY 2006 and FY 2007, appropriated funding levels at only $3 billion in those years would translate into a cut of $1.3 billion and would likely lead to further reductions in future years. You cannot, in other words, consider this year's budget proposal in a vacuum.

Proposed Budget Would Reduce Entitlement Funding to Individual Airports

Before closing, I would be remiss if I did not highlight for the subcommittee the impact that funding at $3 billion could have on the amount of entitlement funds flowing to individual airports across the country. As you know, Congress as part of AIR-21 approved a number of AIP formula changes that are contingent upon AIP being funded at a minimum of $3.2 billion. Under AIR-21, funding at the $3.0 billion level would dramatically reduce funding to commercial service airports, small commercial and non-commercial airports, and certain airports in Alaska. The following offers a glimpse at what this would mean for specific airport categories:

Commercial Service Airports: Under current law, primary airports – those airports with more than 10,000 annual passenger enplanements – receive an AIP entitlement based on the number of enplaned passengers they have in a given year, with a minimum entitlement of $650,000. When AIP is funded at $3.2 billion or higher – as has been the case since FY 2002 – those entitlements double and the minimum entitlement is increased to $1 million. Unless AIP is funded at a minimum of $3.2 billion in FY 2006, entitlements to primary airports could effectively be cut in half from fiscal year 2005 levels and the minimum entitlement paid to nearly 200 airports across the country could be reduced from $1 million to $650,000. Additionally, the overall $600 million cut in program funding would reduce discretionary funding that FAA uses for high-priority projects across the country. It is important to note that these primary airports would see a reduction even if Congress does approve the legislative language the Administration has requested because of separate provisions that proposes to reduce primary entitlements in order to increase the FAA discretionary fund.

Small Commercial and Non-Commercial Airports: Current law also provides grants of up to $150,000 to smaller, non-primary airports in years where the program is funded at $3.2 billion or higher. In FY 2005, more than 2,700 airports received funding under this entitlement. **Funding AIP at $3.0 billion could result in the elimination of the non-primary entitlement in FY 2006.** Additionally, the pool of funding for smaller airports through the Small Airport Fund would be reduced by more than $100 million. Certain airports in Alaska that receive a separate entitlement would also be seriously impacted by a reduction below $3.2 billion.

Conclusion:

Mr. Chairman, as the experiences of this year are proving once again, making the capital investments necessary to prepare our already overwhelmed aviation system for the challenges of the future will not be easy. Also, with globalization, air transportation has become one of the most important engines for economic development and growth contributing an estimated $548.6 billion (Department of Commerce, BEA estimate) to the U.S. economy. A healthy national airport system is vital to our nation's competitiveness.

Airports continue to believe in the fundamental principle that revenues raised by aviation users must be used to pay for aviation system improvements. At the same time, we recognize that increasing budget pressures call for innovative approaches to future system financing, and we are eager to participate in broader discussions about the roles and responsibilities of everyone engaged in the aviation enterprise. We are actively pursuing new approaches to financing airport development, and we look forward to working closely with you and the subcommittee as the debate moves forward.

Statement of Rep. Jon Porter (R-NV)
House Transportation and Infrastructure Committee
Subcommittee on Aviation
Wednesday, May 4, 2005

Mr. Chairman, thank you for holding this hearing today on the financial condition of Aviation Trust Fund.

My purpose here today is to evaluate the financial condition of the Airport and Airway Trust Fund and to talk about, and listen to, possible alternative mechanisms for financing the future needs of our aviation system.

In 1970 Congress enacted the Airport and Airway Development and Revenue Acts. The purpose of which was to address the inadequacy of the nation's aviation system to meet projected growth in air travel. The aviation excise taxes enacted at that time included an increase in the gasoline tax on general aviation, an increase in the passenger ticket tax for domestic flights, a new tax on international commercial passengers, a new tax on air freight waybills, and a new annual aircraft registration tax.

The Trust Fund has been amended, and the caps adjusted over the years dealing Congress's intentions and how the funds could be spent. In FY 2005, the Trust Fund supported 63 percent of the FAA's operations budget. The remainder of the operations budget is provided from the General Fund of the Treasury.

Since its inception, there has been disagreement over how much of the trust fund revenues should be used to pay for FAA operations versus capital investments in the aviation system. Obviously this disagreement continues, otherwise Mr. Chairman none of us would be here today.

Mr. Chairman, I look forward to hearing from our witnesses, and I yield back.

FOR THE RECORD

Statement of Mr. Ronald N. Priddy
President
National Air Carrier Association
Before the
Subcommittee on Aviation
Committee on Transportation and Infrastructure
U.S. House of Representatives
May 4, 2005

Thank you for the opportunity to share the views of the National Air Carrier Association's (NACA's) seventeen member airlines[1] with you concerning the state of the Airport and Airways Trust Fund (Trust Fund).

Chairman Mica and Ranking Member Costello, thank you for holding this hearing as our members have been quite concerned about the state of the Trust Fund. Its health is of the utmost importance to our nation's aviation system and our overall economy.

As you well know, the Trust Fund relies on taxes on the air commerce of this Nation. Everyone flying or shipping in our air transportation system contributes in some manner. Just a few years ago when ticket prices were significantly higher, the state of the Trust Fund was so good that we had the enviable problem of having too much money in the Fund and not enough good programs for investment. This all changed after the terrorist attacks of 9/11. Since these attacks, the overall aviation industry has struggled, suffering massive financial losses. Fewer passengers traveling at significantly lower fares have translated into lower revenue for the Trust Fund and a declining overall balance. Based on the decline, it is possible the Trust Fund could run out of money before the reauthorization in 2007. This comes at a time when we need to make a significant investment in our air traffic system.

The decline of the Trust Fund is due to two primary factors. The first is the decline of revenue from passenger ticket taxes. Low cost carriers like JetBlue and Southwest have been successful in expanding operations at the expense of the "legacy" carriers whose average ticket prices are generally higher. While the passenger ticket tax goes down with the lower price of the ticket, in the past several years traffic has returned to nearly what it was prior to 9/11, and the revenues paid to the Trust Fund are on the increase. That fact is encouraging.

The second factor contributing to the decline of the Trust Fund revenues is a lower General Fund contribution. Thus the Trust Fund is paying FAA expenses that were never intended to be covered by Trust Fund taxes, but are as a General Fund responsibility. The President's FY 2006 budget proposes that almost 89 percent of the Federal Aviation Administration's (FAA's) operating budget come from the Trust Fund. This has been a growing trend over the last couple of years and, if it continues, it threatens to consume all of the Trust Fund balance. This

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[1] Air Transport International, Arrow Air, ATA Airlines, Centurion Cargo Airlines, Champion Air, Express.Net Airlines, Falcon Air Express, Gemini Air Cargo, Miami Air Intl, North American Airlines, Omni Air Intl, Pace Airlines, Ryan Intl Airlines, Southern Air, TransMeridian, USA3000, and World Airways

significantly complicates any long-term planning for capacity improvements and must be corrected immediately.

There have been numerous suggestions from the aviation industry concerning how to fix the problems of the Trust Fund. These ideas have ranged from moving to a user fee-based system similar to that of NavCanada, to initiating commercial bonding schemes, to using peak-hour pricing. There is also significant consensus that the General Fund must pay for those FAA operations not intended to be covered by the Trust Fund. Finally, there is also a general consensus that the FAA needs to operate more efficiently.

On the subject of "user fees", please keep in mind that users are already contributing sufficient revenue to fund the air traffic system, research and development and airport improvements. While these user fees are collected as taxes, we should not lose sight of the fact that users are paying for their air traffic system and services, in full.

NACA strongly believes that the problems of the Trust Fund can and should be fixed by having the federal government pay their fair share to the FAA's budget from the General Fund. The General Fund has provided, on average, 21 percent of the FAA's budget over the last 10 years. It should contribute not less than 20 percent throughout the future. The FAA's budget serves to enable the massive U.S. economy to flourish and grow; provides safety to the flying public, as well as to those on the ground who could be in serious danger if an accident were to occur; and allows the air commerce of this Nation to flow without significant delay. The appropriate level of General Fund contribution must be restored to bring the Trust Fund back into balance.

NACA implores Congress to make sure that the Trust Fund balance is maintained by ensuring that the federal government covers its historic level of funding for the FAA from the General Fund.

Thank you for your time and attention. We would be happy to respond to any written questions by Members of the Subcommittee or full Committee.

Respectfully Submitted
National Air Carrier Association

Ronald N. Priddy
President

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