



The Heritage Foundation

# Background

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## Executive Summary

No. 1289

June 4, 1999

## FAA REAUTHORIZATION: TIME TO CHART A COURSE FOR PRIVATIZING AIRPORTS

*RONALD D. UTT, PH.D.*

Congress is considering legislation to reauthorize the Federal Aviation Administration (FAA). The FAA, an agency of the U.S. Department of Transportation, funds and operates the nation's air traffic control system, enforces federal air safety regulations, provides financial support to U.S. airports, and performs other aviation-related functions. The FAA's authorization expired in 1996, and since then Congress and the President have been trying to work out their differences over the level of funding for the agency.

The main disagreements between the House and the Senate, and between Congress and the President, over reauthorization of the FAA concern how much to spend on aviation programs, how much FAA spending from the aviation trust fund should be supplemented with general revenues, and whether future aviation trust fund spending will be included in federal budget totals and subject to the budget caps agreed upon in the 1997 Balanced Budget Act.

The Aviation Investment and Reform Act (H.R. 1000) sponsored by Representative Bud Shuster (R-PA) proposes that all or more of the revenues flowing into the aviation trust fund be spent by the FAA over the next five years. Although this bill in its original form would have exceeded the fiscal

year (FY) 2000 budget caps, it was amended in late May 1999 to conform to this year's caps, but not to those applicable to fiscal years after FY 2000. Alternatively, the Air Transportation Act (S. 82) introduced by Senator John McCain (R-AZ), as well as the President's plan released in January in his FY 2000 budget proposal, would allow the existing trust fund surplus to accumulate and the spending caps to remain applicable.

Although the President has proposed trust fund spending of \$1.6 billion on the Aviation Improvement Program (AIP) in FY 2000 and S. 82 proposes spending of \$2.8 billion, H.R. 1000 (the House Committee on Transportation and Infrastructure plan) proposes AIP spending of \$2.5 billion in FY 2000 and more than \$4 billion per year between FY 2001 and FY 2004.

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Some Members of Congress object to the buildup of money in the aviation trust fund and contend that all of, if not more than, the revenue now flowing into the trust fund should be spent on airport improvements and other FAA operations. They argue that aviation-related user taxes should be dedicated to aviation and not diverted to other spending programs, deficit reduction, or tax cuts, as has often been the case with other federal trust funds.

Unfortunately, the debate over the mechanism for funding the FAA misses the more critical point: how to improve and reform FAA programs so that they better serve consumers, communities that own the airports, and the economy. For more than a decade, both the media and the government's own watchdogs, such as the U.S. General Accounting Office (GAO) and the Department of Transportation's Office of Inspector General, have reported the failure of the FAA to upgrade its own systems.

The President and Congress also have neglected the obvious opportunities to reform the management and funding of the nation's commercial airports. The privatization of 66 airports around the world in just the past two years demonstrates that large airports can be self-funding, independent of government financial support, and still provide substantial gains to their communities. Despite this record of success, however, some in Congress appear determined to make commercial airports even more dependent on scarce federal dollars by proposing federal airport funding that is more than double that of previous plans.

The airport privatization trend now sweeping the world was pioneered in 1987 by Great Britain when it sold seven airports, including Heathrow and Gatwick, in a public share offering for \$2.5 billion. Since then, the new owner, BAA, plc., has invested more the \$5 billion in the airports, has financed the construction of a passenger rail line connecting Heathrow to downtown London, and last year paid taxes of \$340 million on the profits.

Based on the prices paid by investors for the 66 airports that were sold or leased to private owner/operators over the past two years, many major U.S. airports could be sold for substantially higher prices than Great Britain received for its airports in 1987. These potential sums represent a source of extraordinary untapped wealth for the cities and communities that now own airports. Atlanta's Hartsfield and Chicago's O'Hare airports could be worth as much as \$6 billion each, and Los Angeles International and Dallas-Ft. Worth airports might be worth as much as \$5 billion each. After repayment of debt and federal grants, the proceeds from the sales could be reinvested in other needed community infrastructure, such as schools, wastewater treatment plants, surface transportation improvements, and other public purposes.

Although several U.S. states and cities have attempted to sell or lease their airports to private owner/operators, the Federal Aviation Administration has been an obstacle to these efforts by interpreting certain sections of the U.S. Code governing the relationship between airports and the federal government in ways that make such transactions impossible.

## CONCLUSION

Because the latest extension of the Federal Aviation Administration's authorization is set to expire, it may be too late for Congress to include major FAA reforms in the authorization bills currently under consideration. The two reauthorization bills before Congress differ dramatically in their intent and scope, as well as in the extent to which they would permit fundamental reforms in the future. As a result of these significant differences, S. 82 offers Members of Congress, the President, and state and local officials a better near-term window of opportunity to conduct a comprehensive review of the potential reform options that could allow them to make such reforms operational as early as October 2000.

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*The* Heritage Foundation  
**Backgrounder**

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The main disagreements between the House and the Senate, and between Congress and the President, over reauthorization of the FAA concern how much to spend on aviation programs, the extent to which FAA spending from the aviation trust fund will be supplemented with general revenues, and whether future aviation trust fund spending will be included in federal budget totals and subject to the caps.

The Aviation Investment and Reform Act (H.R. 1000) sponsored by Representative Bud Shuster (R-PA) proposes that all or more of the revenues flowing into the aviation trust fund be spent by the FAA over the next five years. Although the bill in its original form would have exceeded the fiscal

year (FY) 2000 budget caps in the 1997 Balanced Budget Act, it was amended in late May 1999 to conform to this year's caps, but not those applicable to fiscal years after FY 2000. Alternatively, the Air Transportation Act (S. 82) introduced by Senator John McCain (R-AZ), as well as the President's plan released with his FY 2000 budget in January 1999, would allow the existing trust fund surplus to accumulate and the spending caps to remain applicable.

Although the President has proposed trust fund spending of \$1.6 billion on the Aviation Improvement Program (AIP) in FY 2000 and S. 82 would spend \$2.8 billion, H.R. 1000 (the House Committee on Transportation and Infrastructure plan) proposes AIP spending of \$2.5 billion for FY 2000 and more than \$4 billion per year between FY 2001 and FY 2004.

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Some in Congress object to the buildup of money in the aviation trust fund and contend that all of, if not more than, the revenues now flowing into the aviation trust fund should be spent on airport improvements and other FAA operations. They argue that the aviation-related user taxes should be dedicated to aviation and not to other spending programs, deficit reduction, or tax cuts as has often been the case with other federal trust funds. Revenues to the aviation trust fund frequently have been diverted to “deficit reduction” when less was spent on aviation-related funding than the fund had received in dedicated revenues.

Unfortunately, the debate over the mechanism for funding the FAA misses the more critical point: how to improve and reform FAA programs so that they better serve consumers, communities that own the airports, and the economy. For more than a decade, both the media and the government’s own watchdogs, such as the U.S. General Accounting Office (GAO) and the Office of the Inspector General of the Department of Transportation (DOT), have reported on the FAA’s failure to upgrade its systems.<sup>1</sup> The GAO once again has placed the FAA’s air traffic control modernization program on its high-risk list, a distinction shared by such other troubled agencies as the Department of Housing and Urban Development and the Internal Revenue Service.

The President and Congress also have neglected the obvious opportunities to reform the management and funding of the nation’s commercial airports. Indeed, the failure to consider reforming the FAA within the context of the debate over funding could eliminate the likelihood of any real improvements in the foreseeable future.

The privatization of 66 airports around the world in the past two years demonstrates that large airports can be self-funding, independent of government financial support, and still provide sub-

stantial windfall gains to their communities. Despite this record of success, however, some in Congress appear determined to make commercial airports even more dependent on scarce federal dollars by proposing federal airport funding that is more than double that of previous plans.

## THE DEBATE ON AVIATION SPENDING

The Federal Aviation Administration, which is expected to spend just over \$10 billion in FY 1999, is funded by a combination of general revenues from the U.S. Treasury and ten separate dedicated taxes imposed on users of the system. Chief among the user-related taxes are the airline ticket tax, the aviation fuel tax, and the international departure/arrival tax. In addition, depending on which airports they use, air passengers may pay a federally authorized and approved passenger facility charge (PFC) of up to \$3 per flight,<sup>2</sup> which is collected by the airlines and returned to the airport from which the flight originated.

Table 1 lists each of the trust fund’s taxes and the revenues it is estimated that they will provide the fund in FY 1999.

Other user taxes are deposited in the federal Airport and Airway Trust Fund, from which disbursements are made to pay for the various FAA programs, including operation of the air traffic control (ATC) system and grants to airports to build, upgrade, or expand their equipment or facilities. Although the PFC is not considered a federal tax, and the revenues so raised are not deposited in the trust fund, about 10 percent (an estimated \$163 million of the estimated \$1.45 billion the PFC will raise for FY 1999) are passed on indirectly to smaller airports. Large and medium hub airports that choose to implement the PFC (three-fourths of the top 71 airports have done so) must give up 50 cents of trust fund formula grants for every dollar they raise in PFCs.<sup>3</sup> In turn, these

1. U.S. General Accounting Office, *High Risk Series: An Update*, GAO/HR-99-1, January 1999; “The Department of Transportation’s 10 Top Priority Management Issues,” statement of Kenneth M. Mead, Inspector General, U.S. Department of Transportation, before the Subcommittee on Transportation, Committee on Appropriations, U.S. Senate, 106th Cong., 1st Sess., February 1999.
2. The allowable PFC is \$3.00 per flight, up to a maximum of \$12 for a round trip involving connecting flights.

Table 1 B1289

### Estimated Levels of Aviation Taxes Dedicated to Trust Fund, FY 1999

	Billions of Dollars
8% Ticket Tax (to Drop to 7.5% in FY 2000)	\$5.93
\$2.25 Flight Segment Tax (to rise to \$3.00 in FY 2003)	\$1.31
6.25% Tax on Cargo Waybills	\$0.52
Aviation Fuel Taxes	\$1.04*
4.3 Cents per Gallon on Commercial Aviation Fuel	
19.3 Cents per Gallon on General Aviation Gasoline	
21.8 Cents per Gallon on General Aviation Jet Fuel	
International Flight Taxes	\$1.39**
\$12 International Arrival Tax	
\$12 International Departure Tax	
7.5% Tax on "Frequent Flyer" Awards	\$0.14
7.5% Ticket Tax at Rural Airports	\$0.06
<b>Total</b>	<b>\$10.40</b>

Note: \* Includes all three aviation fuel taxes. \*\* Includes both international flight taxes.  
Sources: Budget of the United States Government, FY 2000; Congressional Research Service.

Table 2 B1289

### Recent and Proposed Trust Fund Appropriation Levels

	Billions of Dollars					
	FY 1998	FY 1999 Estimate	President FY 2000	H.R. 1000 FY 2000	H.R. 1000 FY 2001	S. 82 FY 2000
Airport Improvement Program	\$1.70	\$1.60	\$1.60	\$2.48	\$4.00	\$2.48
Facilities and Equipment	\$1.85	\$1.90	\$2.30	*	\$2.50	\$2.19
Research and Development	\$0.20	\$0.15	\$0.17	\$0.15	\$0.15	na
FAA Operations	\$1.90	\$4.10	\$6.04	*	\$6.45	\$5.78
<b>Total</b>	<b>\$5.65</b>	<b>\$7.75</b>	<b>\$10.11</b>	<b>na</b>	<b>\$13.10</b>	<b>\$10.45</b>

Note: \* To be determined as "such sums as may be appropriated." With the exception of spending for S. 82, all spending levels reflect *appropriated* dollars. Levels for S. 82 reflect *authorization* levels subject to subsequent appropriations.  
Sources: Congressional Research Service; H.R. 1000; U.S. Senate Committee on Commerce, Science, and Transportation.



offset grants (called “foregone apportionments”) are reallocated to other projects, mostly at small airports.

The aviation trust fund’s uncommitted balance stood at \$4.3 billion at the end of FY 1998, and President Clinton’s FY 2000 budget estimates that this will rise by \$3.2 billion to \$8.2 billion at the end of FY 2000 from anticipated revenues exceeding the President’s spending proposals.

Table 2 presents current trust fund spending as well as projected FY 2000 spending under both the President’s proposal and the competing proposals (H.R. 1000 and S.82) now under consideration.

Some in Congress have objected to the buildup of money in the aviation trust fund and contend that all, if not more, of the revenues now flowing into the aviation trust fund should be spent on airport improvements and other FAA operations. They argue that the aviation-related user taxes should be dedicated to aviation and not to other spending programs, deficit reduction, or tax cuts. Whereas the President has proposed trust fund spending on the AIP program of \$1.6 billion in FY 2000, the House Committee on Transportation and Infrastructure proposes raising this to an average of \$4.2 billion per year for each of the four years beginning in FY 2001.

Because an increase of this magnitude would either break future budget caps or force harsh cuts in other transportation programs, Representative Bud Shuster, chairman of the House Transportation Committee, is proposing that aviation spending be removed from the budget so that future budget caps no longer apply to aviation trust fund spending. In contrast to the substantially increased spending proposed in H.R. 1000, the Senate proposal to reauthorize the FAA (S. 82) proposes

spending levels in line with current levels, with no change in the program’s budgetary treatment.

The President also is proposing that his recommended FAA spending be funded entirely from trust fund resources. Historically, trust fund resources have been supplemented with general government revenues when this has been necessary to meet the FAA’s spending plans, and this would continue under both S. 82 and H.R. 1000. By eliminating general revenue funding, the President’s budget proposal effectively releases those general revenue funds to be spent elsewhere. Such a diversion of funds is unacceptable to some in Congress who prefer to maintain the status quo, albeit at higher levels of spending.

Exacerbating the dispute between the President and Congress is a higher than expected flow of user taxes into the trust fund because of the healthy economy’s influence on air travel. Such taxes totaled \$8.6 billion in FY 1998 but are expected to rise to \$11.1 billion this year and \$11.6 billion in FY 2000. Many in Congress are reluctant to forego the opportunity this windfall offers for more aviation infrastructure projects back in their districts or states.

In an effort to insulate this windfall from alternative uses by both the President and other Members of Congress, legislation has been introduced to remove the aviation trust fund from the budget and set it up as a separate account with off-budget status. Off-budget status would insulate aviation spending from any fiscal restraint imposed by future budget resolutions and make it off-limits to congressional appropriations committees that must make any spending cuts mandated by the budget resolution. This special protection also would diminish the incentive for Presidents, both now and in the future, to use reductions in federal aviation spending to fund other programs or to facilitate a tax cut.

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3. Robert S. Kirk, “Airport Improvement Program: Airport Finance Issues for Congress,” *CRS Report for Congress*, Congressional Research Service, October 30, 1998, p. CRS-9.

## AVOIDING FAA REFORM

Noticeably missing from the debate between the President and Congress over how much to spend next year on airport projects is any discussion of how the FAA should be reformed and made more efficient so that consumers, the air transportation industry, and the economy are better served. Various government reports and studies have indicated that the FAA's attempt to manage the system's necessary technical upgrades has been a costly failure. "Over the past 17 years," according to the GAO, "the modernization program has experienced cost overruns, schedule delays and performance shortfalls of large proportions."<sup>4</sup> Others peg the misused time at 23 years and the total invested so far at \$43 billion.<sup>5</sup> The DOT's own inspector general recently acknowledged that the program was subject to cost overruns and schedule slippage, and noted that an earlier attempted ATC upgrade—called the Advanced Automated System—was canceled in 1990 after wasting \$1.5 billion.<sup>6</sup>

Beyond its intention to provide the FAA with \$13.1 billion to spend in FY 2001, compared with a projected \$10.2 billion in FY 1999 (FY 2000 proposed totals are still subject to subsequent appropriations), nothing in H.R. 1000 or S. 82 addresses this problem, which has spanned five presidential terms and nine separate Congresses. With neither the President nor Congress proposing anything other than the status quo, the FAA appears destined to add even more years to its lengthy

record of technical mismanagement. Opportunities for fundamental reform, such as those explored earlier in President Clinton's Administration<sup>7</sup> and in the recent restructuring of the Canadian ATC system, are largely ignored.

Similar neglect characterizes attitudes toward the obvious reform opportunities applicable to the management and funding of commercial airports. The privatization of 66 airports around the world in the past two years demonstrates that large airports can be self-funding and independent of government support. Yet some in Congress appear determined to make airports even more dependent on scarce federal dollars by increasing airport funding to \$4.2 billion—more than two and a half times higher than the sum suggested by the President.

Indeed, under H.R. 1000, the incentive for airports to privatize or withdraw from the federal system would be greatly diminished because the new funding apportionment formulas in the bill prom-

Table 3 B1289

### Current and Proposed Apportionment Formulas for Primary Airports

For Each of the:	Current Law	H.R. 1000
First 50,000 Passengers	\$7.80	\$23.40
Next 50,000 Passengers	\$5.20	\$15.60
Next 400,000 Passengers	\$2.60	\$7.80
Next 500,000 Passengers	\$0.65	\$1.95
Passengers in Excess of 1,000,000	\$0.50	\$1.50

Source: Congressional Research Service and H.R. 1000.

4. GAO, *High Risk Series: An Update*.
5. Jeff Plungis, "Small Airports' Ambitions Steer Transportation Bill," *CQ Weekly*, May 1, 1999, p. 996.
6. "The Department of Transportation's 10 Top Priority Management Issues," p. 9.
7. U.S. Department of Transportation, "Air Traffic Control: Analysis of Illustrative Corporate Financial Scenarios," Technical Report prepared by Corporation Assessment Task Force for the Executive Oversight Committee, May 3, 1994.

ise to triple the amount of AIP grants that each existing airport is eligible to receive. Moreover, because such grants account for only 10 percent of funding for large airports, these higher federal funds most likely would displace other non-federal sources that otherwise would be used.

Table 3 presents the current and proposed apportionment formulas that would be applied to airport grants under H.R. 1000. (By way of contrast, S. 82 would maintain current formulas.)

### Tapping into the Aviation Trust Fund

Although the argument raised in defense of these proposals for higher spending and budgetary protection emphasizes the need for airport construction and renovation to keep pace with the booming commercial aviation industry, this rationale is undermined by Chairman Shuster's announced willingness to allow non-aviation transportation projects to tap into the fund in an effort to broaden the proposal's political appeal.<sup>8</sup> Whether this gambit will help to ensure passage of the bill remains open to question, but it certainly has generated a lot of interest among public transit proponents who have rushed forward with costly projects.

In Portland, Oregon, for example, the local transit system has announced that it intends to seek funds generated by the Portland Airport to build a light rail system from the city to the airport. Although Portland voters have twice rejected the project, the proposed diversion of aviation funds to transit would allow revenues generated by airport passenger fees to override local preferences.

Not to be outdone, Senator Charles Schumer (D-NY) has proposed using airline ticket tax revenues generated at New York City's two airports to fund the construction of a Second Avenue subway line in Manhattan. Calling the opportunity a "god-send in every way," the Senator notes that the East Side of Manhattan now has only one subway line (the Lexington), compared with three lines on the West Side.<sup>9</sup> According to press reports, "The construction industry applauded Schumer's vow to tackle mass-transit projects."<sup>10</sup> And well they should: Mile for mile, subways are the costliest form of surface transportation that any community could choose.

Recognizing that even these pork-barrel inducements may not be enough to ensure enactment of his controversial proposal, Representative Shuster announced in late March 1999 that he had reached an agreement with the House leadership whereby he would support the Republicans' FY 2000 budget resolution if they would allow him to bring H.R. 1000 to the floor for a vote. The agreement further provides that if H.R. 1000 does not pass, the excess of aviation user taxes over aviation trust fund spending "would be returned to the traveling public in the form of lower airline taxes."<sup>11</sup> Should it be defeated, or substantially modified in a House/Senate conference committee, Congress would have an opportunity to reconsider and possibly enact a series of far-reaching aviation reforms to reduce federal spending, improve air travel, and provide local communities throughout the country with an infrastructure financial wind-fall.

8. Nancy Oganovich, "Shuster Expresses Support for Plan to Give Transit Share of Aviation Dollars," *BNA Daily Report for Executives*, Internet edition, March 17, 1999. In effect, in an effort to "protect" trust fund monies from being diverted elsewhere, this proposal would allow a limited diversion to some of the most ineffective federal programs in existence. See, for example, Ronald D. Utt, Ph.D., and Wendell Cox, "Transit Pork Has Few Passengers," Heritage Foundation *Executive Memorandum* No. 518, March 27, 1998.
9. Carl Campanile, "Chuck Hops Aboard 2nd Avenue Subway," *New York Post*, April 20, 1999, p. 15.
10. *Ibid.*
11. Jennifer Coderre, "Shuster, House Leadership Reach Agreement on Aviation Funding; Budget Moves Forward," *BNA Daily Report for Executives*, Internet edition, March 25, 1999.



## THE ORIGINS OF FEDERAL AVIATION PROGRAMS<sup>1</sup>

Federal involvement with commercial aviation began in the earliest days of this century when aviation's military potential was first realized.

Federal interest in aviation remained exclusively military until 1918, when the Post Office established an aviation service to provide air mail. The Air Mail Act of 1925 allowed this service to be contracted out to the private sector, and by 1928 this transfer was complete. Then, because the cost of offering air mail to the public exceeded the revenues generated by the service, to the benefit of the budding commercial aviation industry, the Post Office looked for ways to cut contractor fees. In the early 1930s, it encouraged its air mail contractors to carry passengers as a way to help defray costs. Between 1934 and 1938, passenger miles doubled and a new industry emerged, as did several new federal programs to regulate rates and safety—heretofore the responsibility of the Post Office.

The Air Commerce Act of 1926 formalized the federal role in commercial aviation regulation and development, including navigation aids, weather forecasting, safety, licensing, and

investigation of accidents. Although the Act established a well-defined and well-organized process of federal oversight of the industry, it also specifically *prohibited* federal support for airport development. Nevertheless, by the next decade, work relief programs created during the Great Depression led to nearly \$400 million in federal financial support for airport construction.

The Civil Aeronautics Act of 1938 created the Civil Aeronautics Board (CAB) and authorized it to investigate whether the federal government should support airport construction and development. The CAB recommended in 1939 that it should, but not much was done until 1946 because of the interruption caused by World War II.

The Federal Airport Act of 1946 established an airport grant program, and the Airport and Airway Development Act of 1970 established the trust fund financing mechanism and the key elements of the federal aviation program as it exists today. Since 1971, the Federal Aviation Administration has spent about \$139 billion (unadjusted for inflation) in support of commercial aviation.

1. This information is drawn largely from an excellent review of U.S. aviation policy in John W. Fischer and Robert S. Kirk, "Aviation: Direct Federal Spending, 1918–1998," *CRS Report for Congress*, Congressional Research Service, February 3, 1999.

## THE PROPER FEDERAL ROLE IN COMMERCIAL AVIATION

The federal government has supported commercial aviation financially since 1918 and has spent \$139 billion on behalf of the industry just since 1971, when the aviation trust fund was created.<sup>12</sup> There may have been some justification for such extensive direct support in aviation's early years, but the industry's commercial viability

became obvious half a century ago; yet federal financial support for commercial aviation has continued. At the same time, the federal government is still deeply involved in influencing and/or mandating a number of important industry policies that have little to do with the FAA's legitimate role of assuring minimum standards of passenger safety. In fact, some critics have argued that the FAA's dual role of promoting passenger safety and ensuring industry commercial viability leads to

12. John W. Fischer and Robert S. Kirk, "Aviation: Direct Federal Spending, 1918–1998," *CRS Report for Congress*, Congressional Research Service, February 3, 1999.

Table 4 B1289

### Sources of Airport Funding, 1996

	All Airports		Large and Medium Hubs (70)		All Others (3,233)	
	Billions of Dollars	Percentage of Total	Billions of Dollars	Percentage of Total	Billions of Dollars	Percentage of Total
Tax Exempt Bonds	\$4.10	58.0%	\$3.64	65.1%	\$0.47	30.4%
A.I.P. Grants	\$1.37	20.0%	\$0.59	10.6%	\$0.78	50.5%
PFC	\$1.11	16.0%	\$1.01	18.0%	\$0.11	7.2%
State and Local	\$0.28	4.0%	\$0.10	1.80%	\$0.18	11.9%
Other Airport Revenue	\$0.13	2.0%	\$0.26	4.60%	\$0.00	0.0%
<b>Total</b>	<b>\$7.03</b>	<b>100.0%</b>	<b>\$5.58</b>	<b>100.0%</b>	<b>\$1.55</b>	<b>100.0%</b>

Note: Subtotals do not add up to total funding due to rounding and operating loss offsets at small airports amounting to approximately \$100 million.  
Source: General Accounting Office.

inherent conflicts involving tradeoffs that could compromise safety.

Areas of current operation subject to federal involvement that may no longer be necessary include:

- **Financing and regulating** non-safety-related operations of airports;
- **Funding and operating** the air traffic control system;
- **Subsidizing** commercial service to dozens of U.S. communities; and
- **Making** competitive pricing decisions in select markets and non-safety services provided to customers by commercial carriers.

Of all these areas, reform of the federal role in airports and the air traffic control system would

yield the greatest benefits, both in operational efficiencies and in reduced federal spending. Because of space and time constraints, however, this analysis will focus on the federal airport program.<sup>13</sup>

With a few minor exceptions, American airports serving scheduled commercial airlines are publicly owned, usually by a regionally based airport authority which in turn is owned by a city, county, or combination of local jurisdictions. A few, such as Baltimore–Washington International Airport in Maryland, are owned by state governments. Only two—Dulles International and Reagan National—are federally owned, but they are now leased to regional airport authorities that oversee all operations.

Although most airports are locally owned, the federal government has contributed money to their construction and improvements, estimated to amount to over \$26 billion since 1971.<sup>14</sup> The historic accumulation appears substantial; yet on an

13. For more information on opportunities to reform the FAA's Air Traffic Control system, see Robert W. Poole, Jr., and Viggo Butler, "Reinventing Air Traffic Control: A New Blueprint for a Better System" Reason Foundation *Policy Study* No. 206, May 1996, and Wendell Cox and Ronald D. Utt, "How to Close Down the Department of Transportation," Heritage Foundation *Background* No. 1048, August 17, 1995.

annual basis, and compared with other sources of airport financial resources, the federal contribution is relatively small, particularly for the 71 largest airports, which handled 90 percent of the passenger traffic in 1996.<sup>15</sup>

Table 4 indicates that for the 3,300 civilian airports reviewed, federal AIP grants accounted for 20 percent of funding in 1996, with 80 percent coming from other non-federal sources as described. Table 4 also reveals that AIP grants are considerably less important for large airports than they are for smaller ones. In 1996, such grants accounted for just 10.6 percent of funds for the top 71 airports but made up half the funding for the 3,233 smaller airports.

## THE BENEFITS OF PRIVATIZATION

The ability of large airports to tap into non-federal funding sources and develop new ones represents the chief reason why they are candidates for privatization. Even though most might be reluctant at this point to take this step even if it were permitted, many are reported to be willing to forego their federal AIP grant in return for more regulatory freedom in airport operations and the allocation of revenues generated in ways other than those approved by the FAA.

**FAA's Claim to a "Property Right."** Regrettably, as a result of these historic and ongoing investments in locally owned airports, the FAA contends that it has a *de facto* property right, which it has invoked to prevent the sale, transfer, or liquidation of any locally owned airport that received federal funds.<sup>16</sup> It is this claimed property right, combined with the FAA's expansive interpretation of other U.S. statutes governing the federal role in airport operations, that has prevented the privatization of any U.S. airport. (See the Appendix for key portions of the U.S. Code that the FAA has invoked to impede privatization.)

Absent privatization and the financial benefits that privatization provides, commercial airports have no choice but to remain dependent on federal subsidies at a time when commercial airports around the world are being privatized successfully, to the considerable benefit of taxpayers and air passengers. Moreover, by forbidding the exercise of the privatization option, the federal government must continue to support potentially self-sufficient airports despite the many valid alternative uses for such funds.

Although several U.S. cities—notably, Indianapolis and Pittsburgh—have contracted out the management of some or all of their airports' operations to private companies, efforts to sell or lease such facilities in the United States have encountered numerous legal obstacles. The result, of course, is little or no airport privatization activity in the United States. Elsewhere, such activity has been occurring for the past dozen years. In fact, privatization of airports is booming, with nearly 70 airports in Europe, Asia, and South America privatized in the past two years.

### Successful Privatizations in Other Countries.

The first airport privatization occurred in Great Britain in 1987, when the British government sold the British Airport Authority, consisting of seven airports including the major international airports of Heathrow and Gatwick, for \$2.5 billion in a public share offering. The proceeds were used to pay down the national debt. In recognition of the monopoly status this would give the new profit-making owner—BAA, plc.—the contract included a number of stipulations to protect airport users, chiefly passengers and airlines. For example, landing fees for airplanes would be regulated according to a formula that limited annual increases to less than the rate of inflation, ensuring the airlines that such landing fees would decrease in real dollar terms.

14. Fischer and Kirk, "Aviation: Direct Federal Spending," p. 11.

15. U.S. General Accounting Office, *Airport Financing: Funding Sources for Airport Development*, GAO/RCED-98-71, March 1998, p. 7.

16. Although such "rights" are not clearly evident in the federal statutes governing the FAA, FAA contractual grant agreements with airports prohibit the sale or transfer of the airport for up to 20 years, unless explicitly approved by the FAA.

Britain's airport privatization turned out to be highly successful and widely profitable, despite the regulated landing fees. In 1998, BAA, whose major holdings still consist primarily of the British airport properties, earned profits of \$463 million.<sup>17</sup> Since 1987, it has invested over \$5 billion in airport and related infrastructure, including \$750 million in a new rail link connecting Heathrow with London (and the London Underground)—which, incidentally, operates profitably. In the United States, such rail links are built with general tax revenues, revenues from passenger facilities charges that the FAA permits airports to levy under certain circumstances, or from the aviation trust fund itself, as Chairman Shuster has proposed. Moreover, whereas U.S. airports continue to be tax users, British airports have become substantial taxpayers. In 1998, BAA paid \$340 million in taxes on its profits to the British government, as well as millions in property taxes to local governments.<sup>18</sup>

Several other overseas privatizations followed Britain's, notably in Denmark and Austria, and additional facilities in Great Britain; but they accelerated dramatically in the late 1990s: 12 airports in five countries were privatized in 1997, and 51 airports in six countries were privatized in 1998. These transactions took place either through an outright sale (public offering) of all or a portion of the airport or through long-term leases (for 50 to 100 years).

Table 5 lists these airports and provides summary financial information on each transaction.

#### **Benchmarks for Estimating an Airport's Value.**

Column 5 of Table 5 provides the price paid (or the capitalized value of the lease payments) for the airport, and column 6 expresses this price in terms of the number of passengers *enplaned* at the airport each year (adjusted for full or partial ownership). The sale price expressed on a per-enplaned passenger basis generally serves as a proxy or rule of thumb in making rough estimates of what any

other airport might be worth if sold, in much the same way the costs per square foot are used to estimate approximate costs to build a house, shopping center, or any other construction project. Enplaned passengers serve as the generally accepted benchmark in estimating the potential value of airports, because passengers provide an airport's revenues through landings, food and retail sales, parking fees, car rentals, facilities use charges, passenger ticket taxes, and any other service that can be sold to a captive collection of prosperous customers.

The information contained in Table 5 can be summarized and presented in a variety of ways, but the most meaningful presentation for purposes of estimating the likely value of an airport is to categorize the transactions by full and partial sale. It appears from the transactions listed in Table 5 that sharing ownership with a public entity greatly reduces the price per passenger (adjusted for ownership share) that an investor/buyer is willing to pay.

During 1997 and 1998, and for airports serving a million or more passengers per year, partial sales yielded an average per-passenger price of \$81, while the sale or lease of 100 percent of the airport yielded average prices of \$162 per passenger—twice the partial sale rate. This suggests that sales that result in long-term partnerships with a government entity are less valuable than those that do not. For the sale or lease of all airports serving more than a million passengers, the average price per passenger was \$116 in 1997 and 1998.

Of course, these are only benchmark prices, and the final transactions would be subject to a number of adjustments, up or down, for such factors as physical condition of the airport, future growth prospects for the market served, existing contracts with labor and airlines, airline ownership of gates, regulatory mandates, political stability, prospective local taxes, and other factors that may affect an operator's revenues.

17. U.K. GAAP, or \$373 million U.S. GAAP. From BBA, plc., *BAA Annual Review 1997/98*.

18. *Ibid.*

Table 5

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### World-Wide Airport Transaction Prices, 1997–1998

	(1)	(2)	(3)	(4)	(5)	(6)
Airport	Purchaser	Percentage Purchased	Sale Date	Enplaned Passengers (millions)	Purchase Price (\$ millions)*	Price Per Passenger
Birmingham, UK	Aer Rianta	40%	3/97	2.7	\$58	\$53
Bolivia (3 airports) <sup>a</sup>	AGI	NA	3/97	1.2	NA	NA
Brisbane, Aus.	Schiphol	100%	7/97	5.1	\$1,100	\$216
Melbourne, Aus.	BAA	100%	7/97	6.7	\$1,000	\$149
Perth, Aus.	AGI	100%	7/97	2.2	\$495	\$225
Rome, It.	Public Flotation	45%	7/97	11.9	\$344	\$64
Naples, It.	BAA	70%	8/97	1.5	\$32	\$32
Dusseldorf, Ger.	Hochtief / Aer Rianta	50%	1/98	7.5	\$208	\$55
Argentina <sup>b</sup>	Ogden / SEA Milan	100%	2/98	7.8	\$1,400	\$181
South Africa	Aeroporti di Roma	20%	3/98	8.1	\$165	\$102
Adelaide/Parafield, Aus.	Manchester	100%	3/98	1.8	\$238	\$132
Coolangatta, Aus.	Manchester	100%	3/98	1.0	\$70	\$70
Canberra, Aus.	Local Consortium	100%	3/98	0.9	\$44	\$49
Hobart, Aus.	AGI	100%	3/98	0.5	\$24	\$48
Launceston, Aus.	BAA	100%	3/98	0.3	\$11	\$37
Auckland, NZ	Public Flotation	52%	7/98	3.4	\$232	\$132
Wellington, NZ	Infratil	66%	8/98	1.6	\$49	\$47
Mexico <sup>c</sup>	Copenhagen	15%	11/98	4.7	\$116	\$166

Note: \* Purchase price is amount paid for ownership interest (in some cases, less than 100%)

a La Paz, Santa Cruz, and Cochabamba were offered as a 25-year concession with annual rent to be paid; AGI bid 20.8% of gross revenues.

b 30-year concession for 33 airports; "Purchase Price" based upon the present value of guaranteed annual rent payments of \$171.1 million.

c 50-year concession for nine airports including Cancun.

Sources: Frasca and Associates; Reason Foundation.

Table 6 applies these benchmark prices to the top 70 airports in the United States in order to estimate their approximate gross value if sold or leased. In appreciation of the rough nature of these estimates, Table 6 uses the transaction prices from Table 5 to provide three possible values for each airport based on (1) a partial sale, (2) an average for all sales, and (3) a 100 percent sale. These prices are multiplied by the number of 1997 passenger enplanements (the latest available data) to estimate the value of each airport.

It is important to note that these estimates represent gross values and, in addition to the factors cited above, must be adjusted for any of the air-

port's outstanding debt obligations as well as the repayment of the depreciated value of the federal grants received. Because such debt and federal grants can vary substantially from airport to airport, no attempt is made in Table 6 to adjust for the impact these deductions may have on an airport's net asset value.

As Table 6 reveals, the potential gross value of many U.S. airports is extraordinary. Indeed, were these values to be re-estimated with the much higher level of 1999 enplanements, it is likely that Hartsfield (Atlanta) and O'Hare (Chicago) would approach \$6 billion apiece if sold or leased in their entirety.



Table 6

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## Possible Revenue Generated From Privatization of Top 70 U.S. Airports

Airport & Community Served	Passengers Enplaned (1997)	Revenue Generated as Average of Price Where Less Than 100% of Airport Was Sold or Leased	Revenue Generated As Average of All Sold	Revenue Generated as Average of Price Where 100% of Airport Was Sold or Leased
William B. Hartsfield Int'l. (Atlanta, GA)	33,249,963	2,693,247,003	3,856,995,708	5,386,494,006
Chicago O'Hare Int'l. (Chicago, IL)	32,937,402	2,667,929,562	3,820,738,632	5,335,859,124
Los Angeles Int'l. (Los Angeles, CA)	28,874,012	2,338,794,972	3,349,385,392	4,677,589,944
Dallas-Ft. Worth (Dallas, TX)	28,152,220	2,280,329,820	3,265,657,520	4,560,659,640
San Francisco Int'l. (San Francisco/Oakland, CA)	19,284,485	1,562,043,285	2,237,000,260	3,124,086,570
Denver Int'l. (Denver, CO)	16,626,361	1,346,735,241	1,928,657,876	2,693,470,482
Miami Int'l. (Miami, FL)	16,579,269	1,342,920,789	1,923,195,204	2,685,841,578
Newark (Newark, NJ)	15,432,626	1,250,042,706	1,790,184,616	2,500,085,412
Detroit Metropolitan (Detroit, MI)	15,424,000	1,249,344,000	1,789,184,000	2,498,688,000
John F. Kennedy Int'l. (New York, NY)	15,199,099	1,231,127,019	1,763,095,484	2,462,254,038
Phoenix Sky Harbor Int'l. (Phoenix, AZ)	14,940,339	1,210,167,459	1,733,079,324	2,420,334,918
McCarran Int'l. (Las Vegas, NV)	14,631,827	1,185,177,987	1,697,291,932	2,370,355,974
Minneapolis-St. Paul Int'l. (Minneapolis-St. Paul)	14,373,895	1,164,285,495	1,667,371,820	2,328,570,990
Lambert-St. Louis Int'l. (St. Louis, MO)	14,015,360	1,135,244,160	1,625,781,760	2,270,488,320
George Bush Intercontinental (Houston, TX)	13,212,686	1,070,227,566	1,532,671,576	2,140,455,132
Orlando Int'l. (Orlando, FL)	13,044,802	1,056,628,962	1,513,197,032	2,113,257,924
Gen. Edward Lawrence-Logan (Boston, MA)	12,449,466	1,008,406,746	1,444,138,056	2,016,813,492
Seattle-Tacoma Int'l. (Seattle, WA)	12,124,080	982,050,480	1,406,393,280	1,964,100,960
Honolulu Int'l. (Honolulu, HI)	11,596,316	939,301,596	1,345,172,656	1,878,603,192
Charlotte-Douglas Int'l. (Charlotte, NC)	11,334,049	918,057,969	1,314,749,684	1,836,115,938
La Guardia (New York, NY)	10,861,757	879,802,317	1,259,963,812	1,759,604,634
Philadelphia, Int'l. (Philadelphia, PA)	10,777,410	872,970,210	1,250,179,560	1,745,940,420
Pittsburgh Int'l. (Pittsburgh, PA)	10,306,076	834,792,156	1,195,504,816	1,669,584,312
Salt Lake City Int'l. (Salt Lake City, UT)	10,073,021	815,914,701	1,168,470,436	1,631,829,402
Cincinnati (Cincinnati, OH-Covington, KY)	9,322,162	755,095,122	1,081,370,792	1,510,190,244
Reagan Washington National (Washington, DC)	7,537,156	610,509,636	874,310,096	1,221,019,272
San Diego Int'l. -Linbergh (San Diego, CA)	7,131,902	577,684,062	827,300,632	1,155,368,124
Baltimore-Washington Int'l. (Baltimore, MD)	7,008,399	567,680,319	812,974,284	1,135,360,638
Tampa Int'l. (Tampa, FL)	6,588,845	533,696,445	764,306,020	1,067,392,890
Washington-Dulles (Washington, DC)	6,467,195	523,842,795	750,194,620	1,047,685,590
Portland Int'l. (Portland, OR)	6,318,523	511,800,363	732,948,668	1,023,600,726
Ft. Lauderdale (Ft. Lauderdale, FL)	6,088,000	493,128,000	706,208,000	986,256,000
Cleveland-Hopkins Int'l. (Cleveland, OH)	5,710,370	462,539,970	662,402,920	925,079,940
Kansas City Int'l. (Kansas City, MO)	5,376,439	435,491,559	623,666,924	870,983,118
San Jose Int'l. (San Jose, CA)	5,016,667	406,350,027	581,933,372	812,700,054

Source: Heritage Foundation calculations based on Table 5 and the Federal Aviation Administration's ACAIS Database.

Table 6

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## Possible Revenue Generated From Privatization of Top 70 U.S. Airports

Airport & Community Served	Passengers Enplaned (1997)	Revenue Generated as Average of Price Where Less Than 100% of Airport Was Sold or Leased	Revenue Generated As Average of All Sold	Revenue Generated as Average of Price Where 100% of Airport Was Sold or Leased
Luis Munoz Marin Int'l. (San Juan, PR)	4,874,291	\$394,817,571	\$565,417,756	\$789,635,142
Memphis Int'l. (Memphis, TN)	4,871,479	394,589,799	565,091,564	789,179,598
Metropolitan Oakland Int'l. (Oakland, CA)	4,447,833	360,274,473	515,948,628	720,548,946
Chicago Midway (Chicago, IL)	4,426,424	358,540,344	513,465,184	717,080,688
New Orleans Int'l. (New Orleans, LA)	4,300,905	348,373,305	498,904,980	696,746,610
William P. Hobby (Houston, TX)	3,949,236	319,888,116	458,111,376	639,776,232
John Wayne Airport (Santa Ana, CA)	3,820,766	309,482,046	443,208,856	618,964,092
Nashville Int'l. (Nashville, TN)	3,760,270	304,581,870	436,191,320	609,163,740
Indianapolis Int'l. (Indianapolis, IN)	3,574,139	289,505,259	414,600,124	579,010,518
Sacramento Int'l. (Sacramento, CA)	3,495,461	283,132,341	405,473,476	566,264,682
Dallas Love Field (Dallas, TX)	3,413,519	276,495,039	395,968,204	552,990,078
San Antonio Int'l. (San Antonio, TX)	3,343,818	270,849,258	387,882,888	541,698,516
Raleigh-Durham Int'l. (Raleigh-Durham, NC)	3,341,684	270,676,404	387,635,344	541,352,808
Port Columbus Int'l. (Columbus, OH)	3,326,225	269,424,225	385,842,100	538,848,450
Reno-Tahoe Int'l. (Reno, NV)	3,249,535	263,212,335	376,946,060	526,424,670
Albuquerque Int'l. (Albuquerque, NM)	3,149,245	255,088,845	365,312,420	510,177,690
Ontario Int'l. (Ontario, CA)	3,050,750	247,110,750	353,887,000	494,221,500
Robert Mueller Municipal (Austin, TX)	2,948,701	238,844,781	342,049,316	477,689,562
Palm Beach Int'l. (West Palm Beach, FL)	2,898,035	234,740,835	336,172,060	469,481,670
Gen. Mitchell Int'l. (Milwaukee, WI)	2,735,367	221,564,727	317,302,572	443,129,454
Bradley Int'l. (Windsor Locks, CT)	2,684,701	217,460,781	311,425,316	434,921,562
Kahului (Kahului, HI)	2,682,808	217,307,448	311,205,728	434,614,896
Anchorage Int'l. (Anchorage, AK)	2,638,618	213,728,058	306,079,688	427,456,116
Burbank-Glendale-Pasadena (Burbank, CA)	2,356,346	190,864,026	273,336,136	381,728,052
Southwest Florida Int'l. (Fort Myers, FL)	2,191,934	177,546,654	254,264,344	355,093,308
Jacksonville Int'l. (Jacksonville, FL)	2,119,640	171,690,840	245,878,240	343,381,680
City of Colorado (Colorado Springs, CO)	2,080,777	168,542,937	241,370,132	337,085,874
Theodore Francis Green State (Providence, RI)	2,017,782	163,440,342	234,062,712	326,880,684
Louisville Int'l. (Louisville, KY)	1,839,707	149,016,267	213,406,012	298,032,534
Guam Int'l. (Agana, GU)	1,787,504	144,787,824	207,350,464	289,575,648
Tucson Int'l. (Tucson, AZ)	1,775,566	143,820,846	205,965,656	287,641,692
Eppley Airfield (Omaha, NE)	1,732,704	140,349,024	200,993,664	280,698,048
Will Rogers World (Oklahoma City, OK)	1,722,224	139,500,144	199,777,984	279,000,288
Tulsa Int'l. (Tulsa, OK)	1,719,522	139,281,282	199,464,552	278,562,564
El Paso Int'l. (El Paso, TX)	1,634,578	132,400,818	189,611,048	264,801,636
<b>Total</b>		<b>\$46,334,290,113</b>	<b>\$66,355,279,668</b>	<b>\$92,668,580,226</b>

Source: Heritage Foundation calculations based on Table 5 and the Federal Aviation Administration's ACAIS Database.

Again, it must be kept in mind that these are rough estimates based on an average of recent transactions and are subject to a number of adjustments, as briefly discussed above, which may raise or lower the final sale or lease price. However, given the robust prosperity and growth prospects of the U.S. commercial aviation market, a case could be made for above-average prices for some U.S. airports. If, for example, Hartsfield and O'Hare fetch the same average price per passenger as the average of the three Australian airports (\$197 per passenger) privatized in 1997, then each would have been worth about \$6.5 billion in 1997 and as much as \$7 billion in 1999.

Because all but two of the 70 U.S. airports studied are owned by local governments and a few by states,<sup>19</sup> these estimates suggest that some governments are sitting on considerable wealth that could be redeployed to meet other public infrastructure needs, such as surface transportation, school construction and renovation, water supply, and wastewater treatment. The estimated values presented in Table 6 demonstrate that through privatization, local communities can have their cake and eat it too. By cashing out of their airports and letting private companies own and operate them (under contractual guidelines to ensure that the interests of the flying public and the airlines are accommodated), many cities and counties would receive a windfall that could be used to meet other community needs and still receive the services and benefits of the local airport. Moreover, some of this windfall would accrue to the federal government as repayment (of the depreciated value) of the \$26.5 billion in construction grants made since 1971.

## THE LEGAL OBSTACLES TO PRIVATIZATION

Although there is no formal legal prohibition against private airports (3,000 smaller airports are privately owned and operated on a for-profit basis

under FAA regulations) or against the privatization of existing ones, the laws governing airports that receive federal money, as well as contracts with DOT that result from grant agreements, are interpreted by the FAA in ways that effectively preclude such privatization. As noted earlier, any federal investment in an airport, no matter how many years ago it occurred, is interpreted by the FAA as a *de facto* property right that allows the FAA to subject the airport to a series of restrictions that could make privatization economically impossible.

The chief obstacles are the provisions in the Airport and Airway Improvement Act of 1982 (as amended), which require airport owners/sponsors to use all of the revenue generated at the airport for capital and operating needs and explicitly prohibit any diversion of such revenues to non-airport purposes. (See the Appendix for statutory language governing the diversion of aviation revenues.<sup>20</sup>) Although such restrictions against diverting revenues are typical of many federal infrastructure grant programs and are designed to prevent the misuse of federal funds, their repetition in existing law, as well as recent amendments to strengthen them, appear excessive relative to the anti-diversion restrictions applied to other federal infrastructure funding programs.

The primary rationale for these legal prohibitions on grant and revenue diversion is to prevent the grant money, as well as any prospective financial benefits accruing from a targeted federal grant, from being used for non-grant purposes. For example, wastewater treatment grants should be limited to that purpose, and any revenues that flow from the project should remain within that purpose and should not be diverted to pay for roads, schools, or pay raises, as some cities occasionally have done. An example of the diversion of airport revenues would be the imposition of an airline ticket tax on passengers at an airport to fund improvements in its sewer system. More

19. Reagan National and Dulles International airports are owned by the federal government but leased to a local airport authority. Their sale could add several billion dollars to the U.S. Treasury.

20. Specifically, 49 U.S.C. §§ 47101–47133.

recently, the city of Los Angeles has attempted to divert airport revenues to non-airport purposes.

The anti-diversion provisions of federal statutes represent reasonable restrictions to ensure that federal monies are applied to the agreed upon purpose. But the FAA views this prohibition as a perpetual obligation from which a community can never be free, even if it is willing to buy its way out of the obligation by paying back the federal grant.<sup>21</sup> As a result, if an airport were to be privatized, any revenues and profits flowing from the operation of the airport would have to remain within the airport and be reinvested in FAA-approved aviation projects. This, of course, removes any incentive for private investors to acquire an airport. In effect, the FAA appears to be going beyond the law's original purpose of ensuring some measure of integrity for the federal grant-giving process by using the prohibitions to freeze in perpetuity the current organizational structure of the U.S. airport system.

As if the above prohibition on revenue diversion were not enough, the FAA has interpreted these anti-diversion provisions to mean that any revenues generated by the sale or lease of an airport also represent revenues that cannot be diverted to non-aviation purposes. Such an extreme interpretation removes much of the incentive that a community would have to privatize an airport through lease or sale. If actually implemented as a consequence of an airport privatization, it would lead to the peculiar result of reinvesting all of the sale proceeds in the asset just sold, to the considerable benefit of the new private owners who, of course, could never benefit from the windfall because they would be forbidden to take any profits from the operation.

Although the law does not explicitly prohibit privatization, the anti-diversion provisions in the U.S. Code (of which there are at least five) could have the effect of making such privatizations

impossible if interpreted in an expansive fashion. For example:

- **Section 47101(a)(13)** cites "revenues from all sources" as under the restriction, and this could be stretched to include sale proceeds;
- **Section 47107(b)** defines prohibited payments in a way that is general enough to cover sale or lease proceeds;
- **Section 47107(l)(2)** prohibits direct payments or indirect payments other than those reflecting the value of services provided;
- **Section 47111(e)** authorizes the Secretary of Transportation to enforce these prohibitions; and
- **Section 47133** reiterates these restrictions but applies them to an airport that "is" the subject of federal assistance rather than to one that "was," suggesting that if an airport privatizes and relinquishes access to AIP grants, it may no longer be subject to the prohibitions. However, when airports sign a grant agreement with the DOT, the agreement generally runs for the 20 years following the receipt of the grant, potentially making such semantic distinctions irrelevant.

### The White House Role

Just as the general nature of some of these statutes could be used to deter privatization by an administration hostile to the approach, it could be used by an administration sympathetic to privatization to interpret the law in ways that would allow airport privatization to move forward. The administration of President George Bush placed a high priority on infrastructure privatization, and airports were viewed as one of the promising targets. Indeed, so convinced was the Bush Administration that there would be no legislative impediments that it issued an executive order to

21. Specifically, according to the FAA, grant obligations remain in effect for their useful life (usually 20 years) for any facilities that were developed or equipment that was acquired with federal grants, and these obligations shall remain in effect indefinitely for any real property that was acquired with federal grants. See U.S. General Accounting Office, *Airport Privatization, Issues Related to the Sale or Lease of U.S. Commercial Airports*, GAO/RCED-97-3, November 1996, footnote 30, p. 36.

guide the process of infrastructure privatization, with emphasis on airports.

Executive Order 12803 was released on April 30, 1992, to establish an orderly process to guide the privatization of federally funded infrastructure by defining the various federal and state financial claims and the order in which they should be satisfied. The Bush Administration viewed commercial airports as a high priority, and one of the purposes of E.O. 12803 was to provide the Administration's interpretation of the FAA statutes in dispute.

Although E.O. 12803 was implemented by President Bush, the Clinton Administration has not rescinded it; in fact, it has used it on nearly half a dozen occasions to guide the privatization of locally owned wastewater treatment plants that received federal grants from the U.S. Environmental Protection Agency. Moreover, the Clinton Administration's own E.O. 12893, implemented in 1994, affirmed E.O. 12803 and directed federal agencies to seek greater private-sector participation in infrastructure investment and management,<sup>22</sup> and to minimize regulatory and legal barriers to private participation in providing infrastructure facilities and services.<sup>23</sup>

Briefly, Executive Order 12803 specifies that, to the extent permitted by law, sale or lease proceeds are to be distributed in the following manner: (1) Local and state governments shall first recoup in full the unadjusted dollar amount of their portion of the asset's total costs; (2) if sale or lease proceeds remain, the federal government shall recoup the full amount of federal grants associated with the asset, less the applicable share of accumulated depreciation on the asset; and (3) local and state governments shall keep any remaining proceeds if they are used only for investment in additional assets or for debt or tax reduction.

In issuing this order, the Bush Administration believed that its efforts to privatize airports were not in conflict with the statutes and that a reasonable interpretation of them would allow airport privatization to go forward with the assurance that the depreciated value of the federal investment would be repaid. Of course, some in Congress and at the DOT held, and continue to hold, a different interpretation and have used this to discourage or reject privatization proposals.

An argument could be made that the FAA itself, by its deeds and statements, is not always of one mind on the issue. In 1992, for example, the Atlantic City airport was leased to a private contractor and the lease proceeds were diverted to the city's general fund. According to the GAO:

Atlantic City is the only public owner that was able to lease its airport to a private company and collect annual payments to use for non-airport purposes although it had received federal grants. In 1986, the city leased the main airport's terminal and a general aviation field to a private firm for a minimum yearly payment of \$400,000, which was diverted to the city's general fund and not used for airport purposes. We could not determine, nor could FAA explain, why this lease was approved, when the agency has subsequently opposed similar proposals.<sup>24</sup>

Occasional FAA announcements on the issue of airport privatization add to the uncertainty regarding intent. As the GAO reported in late 1996, according to new FAA-proposed policy, "the agency [FAA] will be open and flexible on the conditions for the use of airport revenue if it determines that privatization would not harm the public interest or undermine aviation policy."<sup>25</sup>

22. U.S. General Accounting Office, "Airport Privatization: Issues Related to the Sale or Lease of U.S. Commercial Airports," testimony of Gerald L. Dillingham before the Subcommittee on Aviation, Committee on Transportation and Infrastructure, U.S. House of Representatives, GAO/T-RCED-96-82, February 29, 1996, p. 3.

23. U.S. General Accounting Office, *Airport Privatization, Issues Related to the Sale or Lease of U.S. Commercial Airports*, GAO/RCED-97-3, November 1996, p. 18.

24. *Ibid.*, p. 35.

25. *Ibid.*



Notwithstanding any executive order or the FAA's conflicting actions and statements, in the end it likely will be a court's interpretation that is the deciding factor with respect to whether an airport can or cannot be privatized. But the courts will not have to rule on the issue until someone, whether a mayor or a President, pushes a project forward and induces the litigation likely to bring the issue before the courts.

### **The Pilot Program to Privatize Airports**

If the experience to date under the pilot privatization program authorized by Congress during the last FAA reauthorization is any indication of the reaction of some of the aviation interest groups, such litigation could follow as soon as a city announces its intention to privatize its airport. Under the pilot program enacted during the 1996 reauthorization of FAA, Congress agreed to waive the anti-diversion provisions of the law for up to five pilot privatization projects. However, in order to move forward with an airport privatization, a city or state needed to have the consent of at least 65 percent of carriers serving the airport. So far, no airport serving commercial carriers has been able to garner the necessary consent from a supermajority of the carriers serving it.

Stewart Airport in New York, a small hub airfield providing scheduled service for the several counties just north of New York City, was thought to be a top prospect and had the strong support of New York Governor George Pataki (R). A 99-year lease was agreed to in 1998 at a present value equal to \$133 per enplaned passenger.<sup>26</sup> Unfortunately, the majority of the carriers serving Stewart objected and filed their objections with the FAA, thereby preventing any revenues from being diverted to non-airport uses. New York will divert the proceeds for New York airport purposes, which is an allowable diversion under the federal laws governing airports.

The reluctance of the carriers serving airports to agree to full privatization may be one of the key reasons why so few U.S. airports serving scheduled airlines have taken advantage of the options available under the federal pilot program. Another might be that many local officials are unaware of the option and are therefore unaware of the potential value that their airports possess and the revenues this could yield in support of other city services. Despite privatization activity elsewhere, these events have received little reporting in the mainstream U.S. press.

The aviation trade press, of course, has covered the issue extensively, presenting both sides on a regular basis. But with a readership limited largely to aviation and airport professionals, most of whom benefit from the status quo, such coverage is unlikely to change any minds or induce positive action. In the end, the issue will have to be pushed by local elected officials and their constituents, whose communities will be the chief beneficiaries of the financial windfall that an airport privatization could produce. Until they are informed and energized, as in Indianapolis several years ago and in New York City and New York State today,<sup>27</sup> the issue will languish and opportunities will be lost.

### **WHAT CONGRESS SHOULD DO**

The two FAA reauthorization bills now before Congress differ dramatically in their intent and scope, as well as in the extent to which they would permit fundamental reforms. H.R. 1000 proposes to spend substantially more on airports than would be spent under S. 82 and would make major airports even more financially dependent on federal spending. It also would grant special budgetary privileges that would be difficult to undo in the future; this, in turn, would make it more difficult for future Congresses and Administrations to enact major reforms in airport and air traffic con-

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26. Frasca Associates, facsimile to author.

27. New York City Mayor Rudolph W. Giuliani recently threatened to privatize Kennedy and LaGuardia airports because of dissatisfaction with the Port Authority of New York's management. In February 1999, the mayor issued a formal "Request for Expressions of Interest" to private-sector companies for the management, operations, and development of the two airports.

trol funding and operations. S. 82 does not alter the budgetary treatment now applied to the FAA. H.R. 1000 would reauthorize the FAA through FY 2004, while S. 82 would reauthorize it only through FY 2000.

As a result of these significant differences, S. 82 provides a better near-term window of opportunity for Congress, the President, and state and local officials to conduct a comprehensive review of potential reform options that could allow them to make such reforms operational by October 2000.

## **CONCLUSION**

The FAA authorization bill that prevails will be of critical importance to those who seek fundamental FAA reform, including airport privatization, in the future. The two reauthorization bills now before Congress are dramatically different in their intent and scope, as well as in the extent to

which they would permit fundamental reform in the future. In considering these bills, however, only S. 82 provides Congress, the President, and state and local officials with a better near-term opportunity to conduct a comprehensive review of the potential reform options.

Governors, mayors, and the American people generally would be the chief beneficiaries of an aggressive airport privatization program. Based on recent transaction prices of foreign airports that have been privatized, the privatization of America's airports could provide cities and states with wind-fall financial benefits in the billions of dollars—dollars that could be reinvested in other public infrastructure, such as schools, wastewater treatment, transit, surface transportation, or any other costly project that is a high community priority.

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## APPENDIX

### Provisions of the U.S. Code That Prohibit Diversion of Airport Revenues to Non-Airport Purposes, 49 U.S.C. 47101-47133

**Section 47101(a)(13).** Airports should be as self-sustaining as possible under the circumstances existing at each particular airport and in establishing new fees, rates, and charges, and generating revenues from all sources, airport owners and operators should not seek to create revenue surpluses that exceed the amounts to be used for airport system purposes for which airport revenues may be spent under section 47107(b)(1)....

**Section 47107(b). Written Assurances on Use of Revenue.** (1) The Secretary of Transportation may approve a project grant application under this subchapter for an airport development project only if the Secretary receives written assurances, satisfactory to the Secretary, that local taxes on aviation fuel...and the revenues generated by a public airport will be expended for the capital or operating costs of (A) the airport; (B) the local airport system; (C) other local facilities...substantially related to the air transportation of passengers....

**Section 47107(l)(2). Revenue Diversion.** Policies and procedures to be established pursuant to paragraph (1) [which describes enforcement mechanisms] of this subsection shall prohibit, at a minimum, the diversion of airport revenues (except as authorized under subsection (b) of this section [above] through (A) direct payments or indirect payments, other than

payments reflecting the value of services and facilities provided to the airport....

**Section 47111(e). Action on Grant Assurances Concerning Airport Revenues.** If, after notice, and opportunity for hearing, the Secretary finds a violation of Section 47107(b) of this title, as further defined by the Secretary under section 47107(l) of this title...and the Secretary has provided an opportunity for the airport sponsor to take corrective action to cure such violation...the Secretary shall withhold approval of any new grant application for funds under this chapter, or any proposed modification to an existing grant that would increase the amount of funds made available...and withhold approval of any new application to impose a fee under Section 40117 of this title.... [Section 40117 allows airports to impose the passenger facility charge (PFC).]

**Section 47133. Restriction on Use of Revenues.** (a) Local taxes on aviation fuel...or the revenues generated by an airport that is the subject of federal assistance may not be expended for any purpose other than the capital or operating costs of (1) the airport; (2) the local airport system; or (3) any other local facility that is...substantially related to air transportation....