NATIONAL TAXPAYERS UNION

Issue Brief

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Time for a Broader Horizon

New Report Makes Underwhelming Case for Raising Government Air Travel Charges

It has not taken long for many of the same old debates over infrastructure policy to be rekindled in the new year. One of the most prominent among them is whether to hike the government-mandated Passenger Facility Charge (PFC) on airline tickets. Instituted in 1990, the PFC is intended to fund certain airport capacity and safety projects. Wherever this discussion goes in 2020, policymakers must continue to take a broad, forward-looking view of airport finance, with consumers and taxpayers foremost in their minds.

Introduction: A Longstanding Controversy

The 2018 FAA Reauthorization Act thankfully did not include an increase in the PFC. Instead, lawmakers backing a boost in the fee, including House Transportation and Infrastructure Committee Chair Peter DeFazio, made sure the bill had a door prize: Section 122 of the Act called for an extensive analysis of airport infrastructure, based on 21 specific questions outlined directly in the law.

Key Facts:

- **The Passenger Facility Charge is a mandated fee that adds burdens on air travelers while being poorly structured, not functioning as a true user fee.**
- **Due to PFC's structure, calls to hike the fee or index it to inflation are misguided. Policymakers should instead look to reform the PFC, not increase the burden on travelers.**
- **Section 122 of the FAA Reauthorization Act failed to produce the report that taxpayers and consumers deserved—a report that should have more holistically represented the needs of air travel infrastructure.**

Supporters were likely hoping the 215-page report released recently by the RAND Corporation for the Department of Transportation, would thoroughly vindicate their calls for doubling or even removing the federal cap on the PFC entirely. But the door prize appears to have a lot less luster than they'd hoped it would, making any PFC hike all the less attractive in the omnibus infrastructure bill that House Members are about to release.

For several years NTU has patiently made the case that policymakers have better alternatives for airport finance needs than raising the PFC; this levy that can add nearly $20 to an airline ticket's overall price, depending on the number of enplanements a passenger's itinerary might involve. Aside from reforms that could make airport construction and renovation less costly in the first place, changes to the federal Anti-Head Tax Act could allow a true user fee collected and retained directly by airports to supplant the less accountable PFC.

The RAND Report: A Closer Reading

Although the RAND report does recommend options for a higher PFC, it certainly does not appear to be the chest-thumping endorsement of any approach that some Members of Congress might hope to take. Here we can allow the report to speak for itself.

1) **The Inflation Argument Takes a New Twist.** One commonly employed tactic in favor or a PFC hike is that the amount of the charge—$4.50 per enplanement and up $18 for a round trip—has not been increased since the year 2000, and therefore has eroded due to inflation. Yet because of increases in passenger volume and other factors, actual total PFC collections have more than doubled since 2000, keeping well ahead (more than 50 percent) of inflation.

The RAND report does indeed go on at length about value losses in the per passenger, per segment $4.50 amount due to inflation, but it also makes this interesting observation to the contrary:

> "We are unable to determine whether the value of an individual PFC is eroding faster than airports can benefit from returns to scale. Moreover, to the extent that certain stresses on infrastructure grow in tandem with operations rather than enplanements, and given that larger airplanes have contributed to enplanements growing faster than operations, the erosion of the per-passenger PFC might be less substantial. Put another way, per-plane PFC collections can grow even while the PFC cap stays constant, and if demands on infrastructure are on a per-plane rather than per-passenger basis, the declining purchasing power of the per-passenger PFC would be less consequential."

To be sure, some terminals may need certain capacity improvements if more passengers walk through them, but if planes have gotten more capacious, many other features, such as gates, may not need upgrades at all.

2) **Higher PFCs and More Robust Competition: Still Not Proven.** In hearings last year, supporters of a higher PFC noted that the charge could, by financing more airport infrastructure, allow additional carriers to connect with passengers and foster price-lowering competition. In a May 2019 letter to Chairman DeFazio, four of those upstart low-fare carriers who would supposedly benefit from this calculus disputed such contentions, stating that "Increasing the PFC will not enable more airline competition. To the contrary, it will erode the savings [Ultra Low Cost Carriers] are able to offer over legacy carriers ..."[1]

[1] National Air Carrier Association Letter to the Honorable Peter DeFazio, Chairman, and the Honorable Sam Graves, Ranking Member, Committee on Transportation and Infrastructure, Re: Passenger Facility Charges, May 7, 2019.

Nonetheless, RAND felt obligated to tilt at the windmill and be the first research outfit to try to quantify the impact of PFC on competition. The windmill won. RAND's findings:

> "Overall, our analysis cannot determine whether an individual PFC project affects competition and prices. However, we can conclude that any effects of individual PFC projects are, on average, small relative to other factors, such as local economic conditions and airline hubbing decisions. ...Our conclusions regarding the effects of PFC projects on prices are similar. Overall, the range of uncertainty is relatively large. None of the estimates are statistically different from zero, nor are there clear trends in prices over time before or after PFC project completion. The only clear conclusion is that no single PFC project is likely to significantly alter prices in a particular market."

Once more, a supposed "pro-market" argument for higher PFCs remains insufficiently convincing ... and unproven.

3) For Many Airports, Capital Is Flowing Abundantly. Another contention is that airports lack investment capital for expansion—or at least capital that is relatively cheap to finance compared to levying a higher PFC. Here the RAND report was even-handed, noting that small and medium-sized airports may not offer the kind of stability and return that allows these facilities to count on money streams like bonds for a major source of finance. Yet even if underinvestment from private sources is a problem at some airports, for others bond financing is neither tenuous nor drying up -- and the debt loads from those bonds can be quite manageable. As RAND observed:

"From 2009 to 2017, the amount of debt at year-end for large-hub airports consistently increased, whereas the indebtedness of medium-hub, small-hub, and non-hub airports and nonprimary airports was generally constant. However, the revenue generated by large-hub primary airports increased more than their debt at year-end, meaning that their average debt to- revenue ratio decreased over the period. There is no evidence to suggest that capital flows to airports have declined in recent years or are in jeopardy in the near term. Investment in airport infrastructure at airports with sufficient revenues remains a highly desirable proposition."

4) Trust Fund Surpluses Are Growing. Although the report contained several cautions, RAND essentially agreed that Airport and Airway Trust Fund was flush with cash, and should prudently be drawn down to help fund any legitimate airport needs. Currently the Trust Fund has an uncommitted balance of over $6 billion, which is projected to grow to more than double five years from now in the absence of an economic downturn. RAND's conclusion, while cautious, was nonetheless clear and echoed what many opponents of a PFC hike have been saying for several years:

> "Existing spending guarantee mechanisms in statute are designed to prevent the accumulation of a large uncommitted balance in the AATF and to ensure excise tax revenues are spent on aviation system priorities. In practice, the enforcement mechanism is weak and is regularly ignored by Congress. Under excise tax levels set in current law, a large uncommitted balance is projected to materialize. Congress should take advantage of the existing uncommitted balance to establish and maintain a "rainy day" fund to ensure funding levels can remain stable over time. ... A rainy day fund containing $4 billion to $6 billion would be sufficient to ensure that AATF outflows, for all purposes, can remain stable even in the face of two to three years of severe revenue shortfalls. However, after seeding the rainy day fund, additional revenues should be appropriated to meet clearly identified needs, as determined by the FAA."

According to the Federal Aviation Administration, at its current $4.50 level the PFC is projected to raise nearly $3.7 billion in revenue for 2020. The Joint Committee on Taxation estimates that in 2020, non-interest revenues and transfers to the Airport and Airway Trust Fund will exceed outlays by just over $1 billion. If Congress were to make airport funding mechanisms more flexible to the needs of individual projects (while still retaining oversight of expenditures), these extra monies would amount to the equivalent of a 20 percent boost in PFC collections.

This week Jeff Davis of the nonpartisan Eno Center for Transportation released a more expansive analysis of all Airport and Airway Trust Fund cash flows, one which effectively confirms RAND's recommendation. Davis determined that over the next decade, the Trust Fund could allow for an extra $2.4 billion in average annual outlays while still maintaining this year's $6.8 billion uncommitted balance level. Alternatively, significant tax relief could be provided to passengers and businesses during that same period.

Striking the right balance between flexibility and accountability will take considerable restructuring of federal airport funding, but it is a necessary step for cost effectiveness and the well-being of all stakeholders in the aviation system.

5) The Report's PFC Recommendations Present a Wide Range of Approaches. The More Extreme the Option, the More Caveats RAND Expresses.

Despite the report's intriguing discussion over inflation measurements mentioned above, RAND did propose an upward adjustment to the PFC through any one of four options:

- Index the current $4.50 PFC to some standard price measurement (e.g., construction costs) going forward;
- Raise the PFC cap to $4.75 and index to a standard price measurement, with a corresponding reduction in federal Airport Improvement Program Aid for facilities opting for the higher charge;
- Boost the PFC cap to roughly $7.50, index to a standard price measurement, and require medium and large hub airports to forfeit non-discretionary airport improvement grant funds if they charge the maximum; or
- Lift the PFC cap entirely and allow airports to charge what they wish.

RAND chose option 3 as its preferred prescription, but not without some important qualifications. For one, the report concluded that only a passenger's originating airport—not any layover airport—should be able to levy the new maximum PFC. The rationale:

> "If an airport's PFC increase applies to layover passengers, demand for flights that have layovers at that airport would decrease. This would be particularly problematic for small airports, where almost all routes go through one or two larger 'feeder' airports to connect their community to the national and international system."

In addition, the authors were quick to mention that "although an increase in the PFC cap would likely result in higher ticket prices for passengers traveling through airports that raised their PFC collections, there remains in place a set of guardrails to weigh the public benefits of PFC-funded projects relative to the costs imposed on passengers."

As for the fourth option, RAND expressed serious skepticism, indicating earlier in the report that Canada's uncapped airport charge may be producing negative effects:

> "Per-passenger airport improvement fees at some airports exceed 25 Canadian dollars (or a little less than 20 U.S. dollars as of this writing), and some observers believe that these fees are deterring air travel or causing passengers in close enough proximity to travel by car to the United States in search of lower airfares (Moreau, 2018; Pallini, 2019). An uncapped PFC could have similar consequences if market forces were inadequate to hold down the rate that airports charge."

The PFC's very design works to dampen the positive impact that market forces could have in keeping costs reasonable for passengers. The PFC is administered by the federal government, collected by the airlines, but ultimately remitted to airports. A more market-responsive "user fee" would be levied by airports themselves through technologies such as ticket kiosks, so that customers could more directly hold them accountable for rates and services. Buried on page 164 of the RAND report is yet another reason to think outside of the PFC box: "Under current law, airport sponsors that manage multiple airports can use PFC funds collected at one of their airports to pay for projects at another of their airports. This occurs rarely, *but it challenges the notion that PFCs are a user fee*." (Emphasis added.)

6) **Will Congress Pay Attention to the Rest of RAND's Report?** Advocates for a higher PFC may not want to admit it, but the RAND analysis contains a number of other policy prescriptions that could conflict with their preferred narrative that all airports need to solve their problems is more money. For example:

- The authors call for expanding the airline ticket excise tax to "ancillary services" such as fees for priority board or baggage, but should lower the 7.5 percent rate as the base is broadened to ensure no net tax increase. Will revenue-hungry lawmakers commit to following a revenue-neutral path even as they eye a bigger PFC?

- RAND proposes to end the automatic doubling of AIP primary entitlements per passenger whenever Congress appropriates a certain amount of funding for the program; rather, the FAA should have some discretion in directing grants to higher priority projects. Will Congress forgo its parochial habit of doling out funds to the greatest number of constituencies possible, in favor of a more thoughtful process that better serves the national interest?

- In spite of published FAA guidance, "revenue diversion" of aviation collections to non-aviation purposes remains a major problem, especially among state and local governments that reprogram fuel tax revenues. Is Congress prepared to move forward with genuine solutions involving stricter oversight?

Regrettably, the RAND report gives short shrift to a number of other reforms that could increase transparency, oversight, and efficiency for airports. Although RAND discussed the market pressures that could, in theory, hold airports to a reasonable level of PFC, this small but remarkable passage indicates a missing element: "The FAA does consider whether the scope of each project is justified with respect to existing statute, but the FAA is not responsible for conducting a cost-benefit analysis or any market-based assessment of need." Under a true user fee that airports would have to administer on their own, such analyses or assessments would be likelier, because the consequences of setting an excessive rate would be more immediate. But if Congress insists on retaining the current PFC model instead, what steps will be taken to ensure that such vital information is considered at some level before projects begin? So far there are few clues.

RAND spends just one paragraph on the impact that regulatory burdens can have cost-efficiency of airport projects, and concludes that "This longstanding question in public policy remains a topic ripe for independent, objective, and rigorous analysis to provide Congress and other decisionmakers with clearer direction on how regulations can be harmonized and streamlined." PFC-funded initiatives, for example, are exempt from onerous federal project-labor agreements that can inflate wages paid to construction teams beyond optimal rates, but not exempt from state requirements. Environmental reviews can also impose onerous costs on airports hoping to expand capabilities. A methodical inventory of these maladies and their remedies must be undertaken.

On the subject of inventories, RAND devotes all too little space to a concern NTU had encountered government-wide whenever physical infrastructure is at stake: lack of full knowledge about the number and condition of current assets. Everything from control towers to hangar space can and should be examined thoroughly, but has apparently never occurred. Tellingly, the authors recommended as a starting point a Transportation Research Board study on how to measure "landside" airport infrastructure condition … from 1987 (!). "An up-to-date inventory and assessment of infrastructure conditions would provide a valuable foundation for Congress to make more-informed choices in the future about the levels of investment required across the different infrastructure types," RAND observed. NTU would add that such an analysis should have taken place before lawmakers rendered *any* judgments on additional federal policies to enhance aviation revenues like raising the PFC.

Perhaps the biggest deliberate omission to RAND's airport infrastructure was whether transforming the service component nation's air traffic control (ATC) system into a user-financed, user accountable model (like those in dozens of other nations) would be of benefit to the aviation community. After all, the authors perceptively mentioned that "many aging control towers and other air traffic control facilities require rehabilitation and upgrading" even as airside infrastructure like runways are in largely decent shape. As NTU and its allies have written in the past, ATC reform could help to remove some of the politics from ATC infrastructure funding and rationalize the dedication of resources to where they could make a difference. Alas, RAND stated that "Congressional staff made clear to us that the Section 122 study was not intended to address the infrastructure needs of the more than 300 air traffic control facilities operated by the FAA." Here an old adage best describes this unfortunate situation: mind what you measure, because that is what you will get.

Since the publication of the RAND report, yet another revelation casts a shadow over the thoroughness of its results. To produce its analysis, RAND relied on input from a 16-member "expert panel representing a specified range of stakeholder perspectives" who were credited for their "wealth of experience and insight …". At least one of those panelists, Charlie Leocha who serves as President of Travelers United, believes his organization's "experience and insight" were ignored, apparently in favor of a pro-PFC narrative. Travelers United contends that "airport users such as the localities that benefit from airports 24 hours a day" do not receive sufficient attention in discussions over financing the facilities. In a recent commentary he wrote:

> The first analysis in the study provided an accurate assessment of airport funding. It included airline and consumer concerns as well as airport and locality issues. From that starting point, Travelers United enthusiastically represented passengers. The organization wanted a report that would accurately assess the contributions and taxation of all airport users. The final report provides a complete turnaround from the conclusions initially presented to the participants in the first draft of the study. The final RAND study includes no significant passenger input.

What happened between these first and final drafts to justify such an about-face? The first order of business should be for Congressional proponents of commissioning the RAND study to offer a public explanation. Otherwise, the report's authority will be even further diminished.

Conclusion: Time to Broaden the Policy Horizon

Instead of focusing so heavily on obtaining validation for a higher PFC, Section 122 (and the subsequent report from RAND) should have been written to ensure a more holistic examination of interconnected aviation infrastructure needs. In any case, the resulting "validation," upon closer reading, does not give PFC advocates unfettered "take-off clearance" to rush ahead with their most ambitious plans.

The authors of the RAND report sagaciously wrote that "The ideal airport of 2030 might look quite different from that of 2020." Why then, are so many policymakers concentrating their vision on a single funding tool first implemented in 1990? There is nothing inherently wrong about reaching into the past for good ideas, but the many other reforms discussed here, such as modifying the Anti-Head Tax Act, restructuring Air Traffic Control, and inventorying existing assets, have an even longer pedigree.

On January 29, a $700-plus billion infrastructure plan from House called the "Moving Forward Framework" became only the latest proposal to advocate an increase in the PFC. But if Congress is willing to contemplate the drastic step of massively raising or even uncapping the PFC, it can and should consider fundamental changes to laws and programs that optimize the resources air travelers and taxpayers already contribute. All of the reforms outlined above should be on the table as well. For the sake of everyone in the aviation community and the customers they serve, policymakers must scan the full horizon of possibilities to transform the way Americans fly.

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