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BACKGROUNDER

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End of the Runway: Rethinking the Airport Improvement Program and the Federal Role in Airport Funding

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Abstract

For decades, the federal government has been extensively involved in airport funding through grants and legal restrictions. The Airport Improvement Program (AIP) provides federal grants for capital improvements at public-use airports. The grants are funded primarily by federal taxes on commercial airline passengers and on a number of aviation activities. AIP grants can be used only for certain types of "airside" capital improvements, such as runways and taxiways, and are tied to strict regulations that govern how airports can operate. AIP functions as a middleman scheme that redistributes fliers' resources from the most important airports to those of far less significance. The 60 largest airports in the U.S. serve nearly 90 percent of air travelers. Though these airports have the greatest need for capital investment, these large airports receive only 27 percent of AIP grants. Non-commercial airports—which serve less than 1 percent of commercial fliers—receive about 30 percent of AIP grants. At the same time, the federal government restricts how airports can generate their own revenues through prohibitions in the Anti-Head Tax Act of 1973 and price controls on the Passenger Facility Charge. Instead of continuing this top-down system, Congress should eliminate the AIP, reduce passenger ticket taxes, and reform federal regulations that prohibit airports from charging market prices for their services. These reforms would eradicate the inefficient and inequitable distribution of flier resources and would allow airports to fund capital improvements in a local, self-reliant, and free-market manner.

Key Points

- Every year, the federal government spends over $3 billion on airport improvements through the Airport Improvement Program (AIP), which derives its revenue primarily from taxes on commercial airline passengers and is tied to heavy regulations.
- The AIP harms the vast majority of travelers by redistributing their ticket tax dollars to airports they do not use. Although the top 60 U.S. airports serve nearly 90 percent of air passengers, they receive only 27 percent of AIP funds.
- The federal government prohibits U.S. airports from freely charging their customers, with the exception of administering the highly regulated Passenger Facility Charge (PFC).
- Congress should liberate U.S. airports by eliminating the AIP program, reducing ticket taxes on airline passengers, and reforming federal airport regulations. These reforms would eradicate the inefficient and inequitable distribution of flier resources and would allow airports to fund capital improvements in a local, self-reliant, and free-market manner.

Airports are the backbone of America's aviation system, serving almost 900 million domestic and international passengers in 2015—far more than those of any other country.[1] That number is

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expected to grow significantly: The Federal Aviation Administration (FAA) projects the total number of enplanements to grow to 1.2 billion by 2036.[2]

The federal government has spent billions of dollars funding infrastructure improvements at U.S. airports, mostly through the Airport Improvement Program (AIP), which was authorized in 1970. AIP grants are funded by numerous taxes and fees on fliers and are distributed to airports through a complex system. Yet after billions of federal dollars spent on airports, criticism of the current state of the nation's airport infrastructure continues. Democratic and Republican politicians alike refer to major U.S. airports as "third-world" and call for increasing federal grants to these airports.[3]

These demands for more federal funding ignore the structural problems with how airports are funded and financed in the U.S. The lack of adequate federal grants is not what inhibits airports from building necessary infrastructure and modernizing; rather, the federal government's heavy hand in administering these grants—and the outmoded regulations that accompany them—hampers the development of the nation's airports and harms taxpayers, travelers, and the aviation industry alike.

Calls for spending more through the current middle-man arrangement should be dismissed in favor of reform. Congress and the next President should overhaul airport funding in the following ways:

- **Eliminate** burdensome regulations that restrict how airports can raise and spend revenues;
- **Reduce** costly federal taxes and eliminate inefficient federal grants; and
- **Allow** self-sufficiency and privatization to move U.S. airports towards a modernized, free-market funding system.

This *Backgrounder* details the issues with the current way airports are funded and charts a path forward to allow airports to better make the investments they need to accommodate a 21st-century aviation system.

Background on the Current Federal Role in Airport Funding

Airport Funding and Financing. The nation's most systemically important airports are specified in the FAA's National Plan of Integrated Airport Systems (NPIAS) and are eligible for federal airport funding. The NPIAS designates 3,340 of the nation's 5,136 public-use airports as nationally significant.[4] Airports specified in the NPIAS include the largest public-use commercial and general aviation airports that serve the vast majority of air travel and commerce.[5]

Almost all major commercial airports in the U.S. are publicly owned, either by state or local governments or public entities such as an airport authority.[6] Airport sponsors have several tools at their disposal to finance capital improvements:

- **Airport operation cash flows.** Charges and rents collected from air carriers, airport retail tenants, and other operations;[7]

1. U.S. Department of Transportation, Bureau of Transportation Statistics, "2015 U.S.-Based Airline Traffic Data," BTS 18-16, http://www.rita.dot.gov/bts/press_releases/bts018_16 (accessed November 3, 2016); World Bank, "Air Transport, Passengers Carried," http://data.worldbank.org/indicator/IS.AIR.PSGR?end=2014&start=1970&year_high_desc=true (accessed November 3, 2016).
2. U.S. Department of Transportation, Federal Aviation Administration, *FAA Aerospace Forecast: Fiscal Years 2016–2036*, https://www.faa.gov/data_research/aviation/aerospace_forecasts/media/FY2016-36_FAA_Aerospace_Forecast.pdf (accessed November 3, 2016).
3. Chris Welch, "Joe Biden on LaGuardia Airport: 'I Must Be in Some Third-world Country,'" *The Verge*, February 6, 2014, http://www.theverge.com/2014/2/6/5387148/joe-biden-laguardia-airport-third-world-country (accessed November 3, 2016).
4. In total, there are 19,536 airport facilities in the U.S.: 14,400 are private-use and 5,136 are public-use. The NPIAS includes only public-use airports. U.S. Department of Transportation, Federal Aviation Administration, *Report to Congress: National Plan of Integrated Airport Systems (NPIAS)*, 2016, http://www.faa.gov/airports/planning_capacity/npias/reports/media/NPIAS-Report-2017-2021-Narrative.pdf (accessed November 3, 2016).
5. U.S. Department of Transportation, Federal Aviation Administration, *FAA Aerospace Forecast: Fiscal Years 2016–2036*.
6. U.S. Department of Transportation, Federal Aviation Administration, *Report to Congress: National Plan of Integrated Airport Systems (NPIAS)*, 2016.
7. Fees levied on airlines generally take two forms: (1) a residual agreement, in which the airlines "accept the financial risk and guarantee to provide the airport with sufficient revenue to cover its operating and debt service costs"; or (2) a compensatory agreement, in which the airport assumes the risk of meeting its costs and then charges air carriers a share of the costs based on their use of the airport. See Paul Stephen Dempsey, "Theory and Law of Airport Revenue Diversion," Airport Cooperative Research Program, *Legal Digest*, Issue 2 (May 2008), http://onlinepubs.trb.org/onlinepubs/acrp/acrp_lrd_002.pdf (accessed November 3, 2016).

- **Airport Improvement Program and other federal grants.** Grants from the federal government for capital improvements, derived from taxes on passengers and other aviation activities;

- **Passenger Facility Charges (PFC).** Local charges on passengers levied by the airport, authorized and regulated by federal law and regulations;

- **Commercial debt (bonds).** Tax-free bonds issued by the airport sponsor, usually in the form of General Airport Revenue Bonds (GARBs) or qualified Private Activity Bonds (PABs), and backed by airport revenues;

- **Third-party capital investment.** Air carrier tenants or third parties, such as financial firms, reach an agreement with an airport whereby the third party provides funding for capital improvements, such as Delta Airline's investment in expanding New York's La Guardia Airport;[8] and

- **State and local funding.** Funding provided by state or local governments, usually serving as the matching share for federal grants.[9]

The federal government is extensively involved in most of these mechanisms:

- Congress appropriates the federal grants and the FAA administers them in accordance with statutory requirements and agency policy.

- Congress authorizes airports to levy the PFC, which is capped for each passenger's trip per federal law. The FAA regulates and oversees the use of PFC revenues.

- The federal government exempts interest on municipal bonds, including GARBs, and qualified PABs from federal taxes.[10]

Brief History of Federal Involvement. Following federal involvement in early airports through Post Office operations (for air carriage of mail) and public works programs in the early twentieth century, the federal government became increasingly more involved in airport funding after the taxation of airline passengers was established in the Revenue Act of 1941.[11] Airport funding was provided out of the general fund until the Airport and Airway Development Act of 1970 (Public Law 91–258), which established the Airport and Airway Trust Fund (AATF). The AATF dispenses grants in aid to airports backed by a dedicated funding source of taxes levied on passenger tickets and other aviation-related activities. The current framework of the AATF, including the Airport Improvement Program, was established by the Airport and Airway Improvement Act of 1982 (Public Law 97–248).[12]

Airports' options for raising revenue became more constrained after legal challenges limited airports' ability to levy fees on passengers who use their facilities. In 1970, Delta Airlines sued Indiana's Evansville-Vanderburgh Airport Authority for enacting an ordinance that required airlines to collect a $1 per passenger fee on its behalf and remit the revenues to the airport. Delta claimed that the fee constituted an impediment to interstate commerce, thus violating the interstate commerce clause of the U.S. Constitution. The case was taken up by the Supreme Court in *Evansville v. Delta*, which ultimately ruled against Delta and upheld the constitutionality of a per-passenger fee. The court argued that "so long as the toll is based on some fair approximation of use or privilege for use," and is not "exces-

8. Larry Olmsted, "Delta's New LaGuardia Hub Revolutionary for NYC Fliers," *Forbes*, April 17, 2012, http://www.forbes.com/sites/larryolmsted/2012/04/17/deltas-new-laguardia-hub-revolutionary-for-nyc-fliers/#78d804fd45e5 (accessed November 3, 2016).
9. Dempsey, "Theory and Law of Airport Revenue Diversion."
10. For more on interest exemption, see Curtis S. Dubay, "An Alternative Way to Treat Interest Properly in Tax Reform," Heritage Foundation *Issue Brief* No. 4465, September 30, 2015, http://www.heritage.org/research/reports/2015/09/an-alternative-way-to-treat-interest-properly-in-tax-reform.
11. Charles E. Smith, "Air Transportation Taxation: The Case for Reform," *Journal of Air Law and Commerce*, Vol. 75, No. 4, (December 30, 2010), pp. 915–946, http://www.kslaw.com/imageserver/kspublic/library/publication/12-10journalofairlawsmith.pdf (accessed November 3, 2016).
12. Federal Aviation Administration, "Overview: What is AIP?" September 10, 2013, http://www.faa.gov/airports/aip/overview/ (accessed November 3, 2016).

sive in comparison with the governmental benefit conferred[,]" then the passenger fees did not "discriminate[] against interstate commerce and travel," and are legal.[13]

Although the local airport charges passed constitutional muster, they subsequently faced an even greater challenge from special interests in Congress. In a classic case of cronyism, Delta and other air carriers successfully lobbied Congress to decide that, *contra* the Supreme Court, per-passenger fees did inhibit interstate commerce. The lobbying resulted in the enactment of a provision that prohibited passenger fees at airports in the Airport Development Acceleration Act of 1973 (Public Law 93–44). Commonly known as the Anti-Head Tax Act, section 7 of the act (49 U.S. Code 40116) states that no state or local government shall

> levy or collect a tax, fee, head charge, or other charge, directly or indirectly, on persons traveling in air commerce or on the carriage of persons traveling in air commerce or on the sale of air transportation or on the gross receipts derived therefrom.[14]

This prohibition limited airports' ability to achieve self-sufficiency and solidified their reliance on federal grants and other regulated means of revenues for capital funding.

Federal Taxes and Fees on Aviation. Passengers now pay a variety of federal taxes that are deposited in the AATF. These revenues are then used for FAA operations (including the provision of Air Traffic Control services) and directed by Congress back to airports through grant programs, primarily the Airport Improvement Program. AATF taxes and fees include:

- 7.5 percent domestic passenger ticket tax (including a tax on the value of mileage awards);
- $4 per passenger domestic flight segment tax (indexed to the Consumer Price Index);
- $17.80 per passenger tax on international arrivals and departures (indexed to the Consumer Price Index);
- $8.90 per passenger tax on flights to Alaska and Hawaii (indexed to the Consumer Price Index);
- 6.25 percent tax on the value of domestic cargo transported by air; and
- Aviation fuel taxes:
  - Domestic commercial fuel: $0.043 per gallon;
  - Domestic general aviation gasoline: $0.193 per gallon; and
  - Domestic general aviation jet fuel: $0.218 per gallon (plus a $0.141 per gallon surcharge for fuel used in a fractional fleet aircraft).[15]

On average, the Government Accountability Office (GAO) found that federal taxes and fees comprise 13.7 percent of the cost of a domestic ticket (excluding fuel taxes), or roughly $55 on a $392 domestic round trip ticket, the 2014 national average.[16] In total, these taxes brought in $14.3 billion in AATF revenues in fiscal year (FY) 2015, roughly 95 percent of which was derived from taxes levied on commercial passengers.[17]

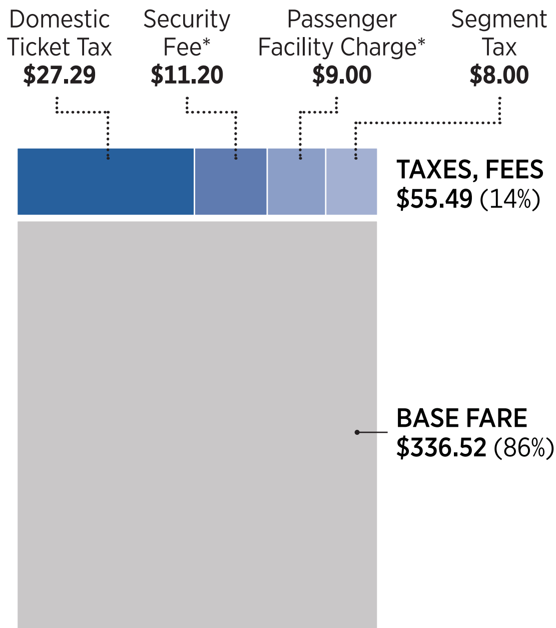
Airport Improvement Program. The Airport Improvement Program (AIP) is the principal federal grant program for airport improvements, totaling $3.35 billion per year since 2012.[18] Since 1992, Congress has authorized over $75 billion for the Airport Improvement Program, resulting in appropriated grants totaling nearly $70 billion over the same

13. *Evansville v. Delta*, 405 U.S. 707 (1972).
14. Airport Development Acceleration Act of 1973, Public Law 93–44.
15. Federal Aviation Administration, "Airport and Airway Trust Fund," *Fact Sheet*, https://www.faa.gov/about/budget/aatf/media/AATF_Fact_Sheet.pdf (accessed November 3, 2016).
16. U.S. Government Accountability Office, *Raising Passenger Facility Charges Would Increase Airport Funding but Other Effects Less Certain*, GAO-15-107, December 2014, http://www.gao.gov/assets/670/667444.pdf (accessed November 3, 2016).
17. Federal Aviation Administration, "Airport and Airway Trust Fund."
18. FAA Modernization and Reform Act of 2012, Public Law 112–095.

CHART 1

Breakdown of Airplane Ticket Taxes and Fees

For a typical round-trip ticket from Dulles Airport to Dallas/Fort Worth:



* Funds do not go to Airport and Airway Trust Fund.
SOURCES: Heritage Foundation calculations based on data from the Federal Aviation Administration, "Airport and Airway Trust Fund (AATF) Fact Sheet," https://www.faa.gov/about/budget/aatf/media/AATF_Fact_Sheet.pdf (accessed October 11, 2016), and Federal Aviation Administration, Bureau of Transportation Statistics, "Annual U.S Domestic Average Itinerary Fare in Current and Constant Dollars," http://www.rita.dot.gov/bts/airfares/programs/economics_and_finance/air_travel_price_index/html/AnnualFares.html (accessed October 25, 2016).

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period.[19] The GAO found that AIP grants make up a substantial share of funding for airport development, accounting for 33 percent of capital funding on average.[20] The grants are relatively inflexible, limited only to certain eligible projects, mainly consisting of "airside" developments, such as runways and taxiways.[21] AIP funds cannot be used for ineligible "landside" projects, such as maintaining or operating buildings and making improvements to attract commercial enterprises. Some projects—including, notably, the construction of terminals and gates—can only be partially funded by the AIP, as certain airside aspects of terminals are eligible, but landside portions are not.[22]

The distribution of AIP grants is intricate and relatively opaque to the average ticket-taxpayer who is supposed to benefit from the funded projects. Grants are delivered primarily through three different mechanisms:

1. Entitlements (Formula Funds). Entitlement AIP grants are apportioned by formula to airports and represent roughly 65 percent of total AIP grants. The entitlements are provided to four different types of recipients:

1. Primary airports,
2. Cargo service airports,
3. General aviation airports, and
4. Alaska supplemental fund.

The entitlement grants heavily favor smaller airports at the expense of larger ones. For example, the formula allocates funding on a passenger boarding basis that declines as annual boardings increase, awarding $7.80 for each of the first 50,000

19. Bart Elias and Rachel Yang, "Issues in the Reauthorization of the Federal Aviation Administration (FAA)," Congressional Research Service *Report For Congress* No. 43858, January 29, 2015, http://www.cq.com/pdf/crsreports-4619754 (accessed November 3, 2016); U.S. Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2017: Department of Transportation* (Washington, DC: U.S. Government Publishing Office, 2016), https://www.whitehouse.gov/sites/default/files/omb/budget/fy2017/assets/dot.pdf (accessed November 3, 2016).
20. Rachel Yang and Robert Kirk, "Financing Airport Improvements," Congressional Research Service *Report for Congress* No. 43327, March 24, 2016, http://www.cq.com/pdf/crsreports-4862830 (accessed November 3, 2016).
21. Projects that are funded by AIP are limited to airport planning, airport development, noise compatibility planning, and noise compatibility projects. The eligibility of all AIP projects is contingent on meeting specific requirements for the type of project and 15 general project requirements as outlined in the AIP Handbook. See U.S. Department of Transportation, Federal Aviation Administration, *Airport Improvement Program Handbook*, September 30, 2014, https://www.faa.gov/airports/aip/aip_handbook/media/AIP-Handbook-Order-5100-38D.pdf (accessed November 3, 2016).
22. Ibid.

passengers, but only $0.65 for each passenger over 500,000 and $0.50 for each passenger in excess of 1 million. Furthermore, airports that administer a PFC over $3 (which is nearly all of the nation's major airports) must forgo 75 percent of their entitlement funding. Then 87.5 percent of those forgone entitlement grants is placed in the Small Airport Fund.[23]

In addition, general aviation, reliever, and non-primary commercial airports receive about 30 percent of AIP funds, despite constituting a minimal portion of commercial activity (less than 1 percent of all boardings in total) and thus a small share of AATF tax revenues.[24] Furthermore, general aviation airports primarily serve few individuals in comparison to the aviation system as a whole. For example, 29.5 percent of general aviation hours were designated as personal use (recreational flying and tourism), while 19.7 percent were attributed to corporate, executive, or business travel.[25] Heavily subsidizing these airports comes at the expense of the larger airports that serve the vast majority of taxpaying air travelers and face the largest congestion challenges. These shortcomings will be discussed in further detail in the subsequent section.

2. State Block Grants. The State Block Grant Program accounts for 20 percent of total AIP funding. This program provides funding directly to states, which then assume responsibility for administering the grants to "other than primary" airports, consisting of non-primary commercial service, reliever, and general aviation airports.[26] Participation is limited to 10 states, and the states must comply with additional grant assurances (discussed below) regarding the administration of the grants.[27]

3. Discretionary Grants. The remaining funds not distributed via apportioned entitlements or the State Block Grant Program, as well as the 12.5 percent of forgone AIP grants under the PFC program, are distributed at the discretion of the FAA. Discretionary grants represent about 15 percent of total AIP funding and are based on project priority and other criteria. A certain portion of discretionary grants must be set aside for three particular types of projects:

1. Airport noise set-asides (35 percent of discretionary funding);
2. Military airport program (at least 4 percent); and
3. Grants for reliever airports (0.66 percent).[28]

AIP Grant Assurances. AIP grants come with considerable strings attached. Airport sponsors (i.e., the owner of the airport) that receive AIP funds are required to accept terms and conditions known as Grant Assurances, as required by Congress[29] and implemented by the FAA. These grant assurances require airports to comply with rules governing how the airport may operate and conduct business. While most grant assurances remain in full effect for the "useful life of the facilities developed or equipment acquired"—not to exceed twenty years—two major grant assurances apply *permanently* to any airport that has accepted AIP funding:[30]

1. **Revenue diversions.** This Grant Assurance prohibits any revenue generated by airport activities

23. Yang and Kirk, "Financing Airport Improvements."
24. Ibid., and U.S. Department of Transportation, Federal Aviation Administration, "Passenger Boardings, Rank Order, and Percent Change from 2014," September 28, 2016, https://www.faa.gov/airports/planning_capacity/passenger_allcargo_stats/passenger/ (accessed November 3, 2016).
25. U.S. Department of Transportation, Federal Aviation Administration, *Report to Congress: National Plan of Integrated Airport Systems (NPIAS)*, 2016.
26. U.S. Department of Transportation, Federal Aviation Administration, "State Block Grant Program," *Factsheet*, September 23, 2016, http://www.faa.gov/airports/aip/state_block/ (accessed November 3, 2016).
27. Current participating states include: Georgia, Illinois, Michigan, Missouri, New Hampshire, North Carolina, Pennsylvania, Tennessee, Texas, and Wisconsin. See U.S. Department of Transportation, Federal Aviation Administration, "State Block Grant Program."
28. Elias and Yang, "Issues in the Reauthorization of the Federal Aviation Administration (FAA)."
29. 49 U.S. Code § 47107.
30. U.S. Department of Transportation, Federal Aviation Administration, "Assurances: Airport Sponsors," B.1, 2014, https://www.faa.gov/airports/aip/grant_assurances/media/airport-sponsor-assurances-aip.pdf (accessed November 3, 2016).

from funding projects unrelated to the operating and capital costs of the airport or other airport uses.[31]

2. **Exclusive rights.** Airport sponsors are prohibited from establishing an "exclusive right for the use of the airport by any persons providing, or intending to provide, aeronautical services to the public."[32] This Grant Assurance bars airports from denying any duly qualified party an opportunity to provide services at their airport, and is augmented by another assurance that bars economic discrimination of air service providers.

While these permanent assurances serve some stated federal goals, their restrictive nature has created various market distortions, limits airports' ability to innovate, and impedes efforts for airport privatization. The problems posed by these restrictions will be discussed further in the subsequent section of this paper.

Passenger Facility Charges. Due to the limitations Congress placed on airports' ability to collect revenues, by the 1990s many of the nation's largest airports required more revenues to finance capital improvements than AIP could provide. This led Congress to make an exception to the Anti-Head Tax Act in 1990, allowing airports to levy a local PFC. Congress set a limit on the maximum PFC an airport can charge per passenger, originally at $3 per passenger with a maximum of $12 per round trip. In 2000, Congress raised the ceiling to $4.50 per airport and $18 per round trip, where it remains today.[33] Because the PFC ceiling was not indexed to inflation, its purchasing power has eroded since 2000, and many airports and travel advocates have called for an increase in the cap or its outright elimination.[34]

Like the AIP, PFCs come with strings attached. PFC revenue can be used only for "FAA-approved projects that enhance safety, security, or capacity; reduce noise; or increase air carrier competition."[35] Furthermore, participating airports must prove to the FAA that they could not complete their capital projects with existing revenues. In addition, large and medium hubs must forgo 75 percent of their AIP entitlement grants if the PFC is fully utilized.[36] However, although PFC revenues are restricted, they can be used for a much wider variety of causes than AIP grants, including paying off interest on bonds (to which airports devote approximately 44 percent of PFC revenue) and the landside costs of terminal construction.[37]

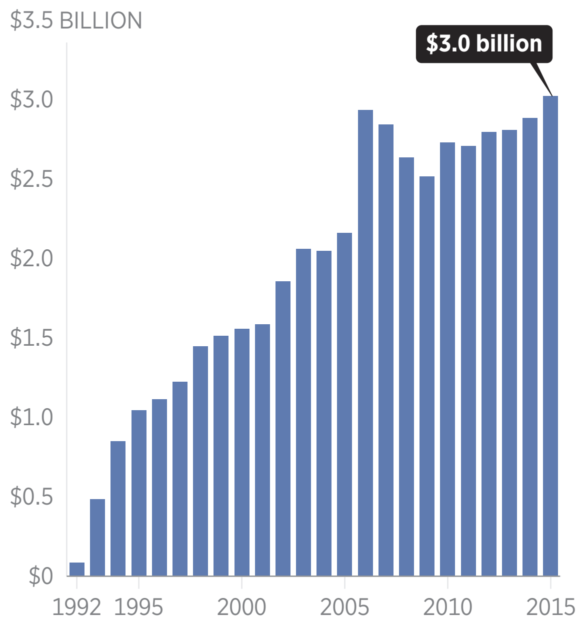
Because of the greater flexibility and availability of PFCs in comparison to federal grants, PFCs are an important and growing source of revenue for the nation's most vital airports. Ninety-five of the largest 100 airports use PFCs, almost all at the maximum level of $4.50. This includes all of the large hubs—which handle 73 percent of the nation's enplanements.[38] PFC collections hit an all-time high in 2015, totaling $3.022 billion, and are expected to continue growing.[39]

31. Twelve airport authorities are exempted from FAA restrictions on the use of airport revenues because they had preexisting agreements with the FAA prior to the Airport and Airway Safety and Capacity Expansion Act of 1987 (Public Law 100–223), when these restrictions were extended. They include many major airports, including those managed by the Port Authority of New York and New Jersey (JFK, Newark, LaGuardia, and Teterboro airports), City of Chicago (Chicago O'Hare and Midway Airports), and Massachusetts Port Authority (Boston-Logan and Hanscom Field Airports). See U.S. Department of Transportation, Federal Aviation Administration, *Airport Compliance Manual—*Order 5190.6B: Airports, Chapter 15, September 30, 2009, http://www.faa.gov/airports/resources/publications/orders/compliance_5190_6/ (accessed November 3, 2016).
32. Ibid.
33. Rachel Yang and Robert Kirk, "Financing Airport Improvements."
34. Press release, "Leaders From 125-Plus Airports Sign Letter to Congress Asking for Modernized PFC," American Association of Airport Executives, March 25, 2015, https://www.aaae.org/aaae/AAAEMemberResponsive/Press_Releases/2015/Leaders_From_125-Plus_Airports_Sign_Letter_to_Congress_Asking_for_Modernized_PFC.aspx (accessed November 3, 2016).
35. U.S. Department of Transportation, Federal Aviation Administration, "Passenger Facility Charge Program," September 14, 2016, http://www.faa.gov/airports/pfc/ (accessed November 3, 2016).
36. Rachel Yang and Robert Kirk, "Financing Airport Improvements."
37. Ibid.
38. U.S. Department of Transportation, Federal Aviation Administration, "Passenger Facility Charge (PFC) Monthly Reports," October 31, 2016, https://www.faa.gov/airports/pfc/monthly_reports/ (accessed November 15, 2016).
39. U.S. Department of Transportation, Federal Aviation Administration, "Key Passenger Facility Charge Statistics, 1992–2015," https://www.faa.gov/airports/pfc/monthly_reports/media/stats.pdf (accessed November 3, 2016).

CHART 2

Adding Up Facility Fees

Since 1992, Passenger Facility Charges levied on fliers have generated nearly $47 billion for airport improvements.



NOTE: These figures reflect final PFC collections, after corrections have been made to preliminary airport reports. The spike in collections in 2006 is attributable to an FAA decision to allow airports to correct for errors in all previous years' preliminary reports, resulting in $400 million in corrections from various prior years assigned to 2006.
SOURCE: Federal Aviation Administration, "Key Passenger Facility Charge Statistics," https://www.faa.gov/airports/pfc/monthly_reports/media/stats.pdf (accessed October 13, 2016).

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Contrary to some who liken it to a federal tax, the PFC is a local fee collected by the airlines and remitted to the airport.[40] The federal government is only involved because it inserted itself into the marketplace via federal law (Anti-Head Tax Act) and the subsequent exception for PFCs, which are also capped by an act of Congress.

Problems with the Current Funding Regime

The current system of funneling passenger taxes through the federal government and back to airports via a politically directed mechanism makes little economic sense and has proved detrimental to airports and the aviation system. In particular, the current tax-and-spend scheme—along with its associated regulations—has had the following negative effects on the aviation industry and its patrons:

Market Distortions and Misallocation of Resources. The current system's most egregious effect is the siphoning of funding from the airports that serve the most travelers and require the most investment to those that move the fewest. The effect has been an allocation of resources that would never occur in a normally functioning market.

The largest airports in the country consist of large and medium hub airports as designated in the FAA's National Plan of Integrated Airport Systems.[41] The 30 large hub airports account for 72.5 percent of all enplanements in the U.S.; 30 medium hubs account for 15.4 percent of U.S. enplanements.[42] Together, these 60 airports account for 88 percent of commercial enplanements—representing the overwhelming majority of commercial activity.[43]

Despite these airports serving nearly all commercial air traffic, they received only 27 percent of AIP grant distribution in FY 2015.[44] Because taxes on commercial passengers account for nearly 95 percent of federal AATF taxes and commercial passen-

40. E.g., Grover G. Norquist, Americans for Tax Reform, letter to the U.S. Congress, March 26, 2015, http://www.atr.org/sites/default/files/assets/PFC%20Letter.pdf (accessed November 3, 2016).

41. The FAA's definition of a "hub" airport is contingent on the airport's percentage of national enplanements. See: U.S. Department of Transportation, Federal Aviation Administration, *Report to Congress: National Plan of Integrated Airport Systems (NPIAS)*.

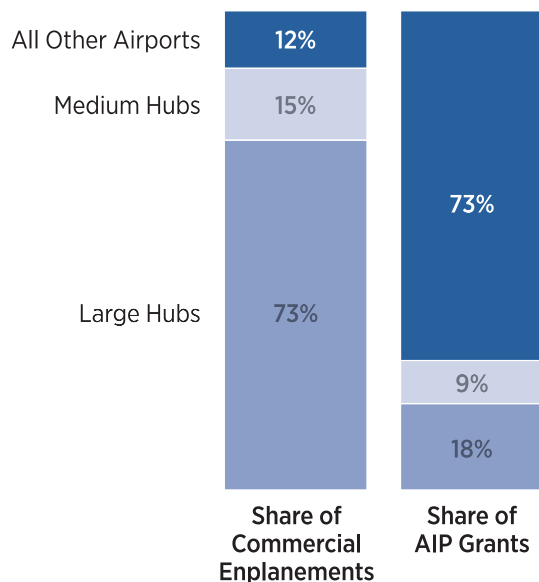
42. The FAA categorizes large hub airports as those that account for one percent or more of total national enplanements, while medium hubs each account for 0.25 to 1 percent of national enplanements. U.S. Department of Transportation, Federal Aviation Administration, *Report to Congress: National Plan of Integrated Airport Systems (NPIAS)*, 2016; U.S. Department of Transportation, Federal Aviation Administration, "Passenger Boardings, Rank Order, and Percent Change from 2014."

43. U.S. Department of Transportation, Federal Aviation Administration, "Passenger Boardings, Rank Order, and Percent Change from 2014."

44. Yang and Kirk, "Financing Airport Improvements."

CHART 3

Aiport Improvement Program (AIP) Redistributes Funding to Smaller Airports



NOTES: Enplanements are for calendar year 2015, while AIP grants are for FY 2015. Because AIP allocates funding to airports that do not serve commercial passengers (i.e., cargo, general aviation), the "All Other Airports" category includes these non-commercial airports in the "Share of AIP Grants" data set. However, these non-commercial airports contribute a fairly trivial share of revenues to the AATF.

SOURCES: Federal Aviation Administration, "Passenger Boarding (Enplanement) and All-Cargo Data for U.S. Airports," http://www.faa.gov/airports/planning_capacity/passenger_allcargo_stats/passenger/ (accessed October 12, 2016), and Rachel Y. Yang and Robert S. Kirk, "Financing Airport Improvements," Congressional Research Service *Report for Congress* No. 43327, updated March 24, 2016, http://www.cq.com/pdf/crsreports-4862830 (accessed October 27, 2016).

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gers primarily fly through these large airports, this represents a massive transfer of funding to airports that are significantly less important to the aviation system.[45] The system further favors small airports by allowing AIP grants to fund a larger share of project costs at small airports: Grants to large and medium hubs are capped at a 75 percent share of project costs (80 percent for noise-reduction projects), while the federal share for all other airports is 90 percent to 95 percent.[46] This diversion of money from the most traveled airports to the least traveled ones—along with the limitation on what revenues the large airports can raise themselves—makes little sense given that the need to alleviate congestion and accommodate a large volume of passengers is greatest at these large airports.

The federal aviation tax system has led to smaller inefficiencies. While many decry the rise of ancillary air carrier fees (e.g., baggage fees) on top of ticket taxes, the air carriers are able to keep base prices low by levying these additional services, in part because the base ticket price is taxed exorbitantly while the ancillary fees are not. That provides an incentive for the air carriers to make up their costs in other areas that are not as heavily taxed in order to keep base prices affordable. Furthermore, the federal Anti-Head Tax Act results in odd situations such as rides on tethered hot air balloons being eligible for state sales taxes, but sales taxes on trips made on balloons that are not tethered to the ground are forbidden.[47]

Costs of Federal Bureaucracy and Restrictions. Airports should be able to derive their own revenue and be self-sufficient just like any other business. Relying on the federal government's continued involvement through grants and regulations for funding has hampered airports with a host of wide-ranging downsides. Because grant funding carries many federal requirements, airports must spend a large amount of time and resources navigating the large federal bureaucracy and conforming to various federal regulations, including those imposed on general airport practices, use of revenue,

45. Ninety-five percent includes revenues derived from transportation of persons, use of international air facilities, and a portion of aviation fuel for commercial use. Heritage Foundation calculations based on Federal Aviation Administration, "Airport and Airway Trust Fund."

46. Bart Elias and Rachel Yang, "Federal Civil Aviation Programs: In Brief," Congressional Research Service *Report for Congress* No. 42781, September 27, 2016, http://www.cq.com/pdf/crsreports-4971484 (accessed November 3, 2016).

47. Jared Walczak, "Can States Tax Your Hot Air Balloon Ride?" Tax Foundation, The Tax Policy blog, July 24, 2015, http://taxfoundation.org/blog/can-states-tax-your-hot-air-balloon-ride (accessed November 3, 2016).

TABLE 1

Airport and Airway Trust Fund Revenues, FY 2015

Paid by commercial passengers

Component	Revenue (millions)	Share of Total
Transportation of Persons	$9,838	69.0%
Use of International Air Facilities	$3,311	23.2%
Transportation of Property	$497	3.5%
Aviation Fuel (Commercial Use)	$411	2.9%
Aviation Fuel Other than Gas (Non-commercial)	$174	1.2%
Aviation Gasoline	$22	0.2%
Liquid Fuel Used in a Fractional Ownership Flight	$15	0.1%
Total	$14,268	100.1%

NOTE: Percentages sum to more than 100 due to rounding.
SOURCE: Federal Aviation Administration, "Airport and Airway Trust Fund (AATF) Fact Sheet," https://www.faa.gov/about/budget/aatf/media/AATF_Fact_Sheet.pdf (accessed October 13, 2016).

land acquisition, and providing opportunities for small businesses.[48]

These regulations require that the government approve the layout design of the airport and any alterations made to it, and that at least 10 percent of retail businesses at the airport are small business concerns (as defined by the government).[49] One overtly specific pending proposal would require that airports provide lactation areas for nursing mothers that have "a place to sit, a table or other flat surface, and an electrical outlet."[50] Airports must focus a great deal of resources simply complying with this mountain of federal regulations instead of running the airport as a business. Furthermore, these restrictions hinder each airport's ability to tailor its development to its own unique needs.

In addition, broader federal regulations concerning federal spending are associated with increased costs for the construction of new projects.

- "Buy America" provisions require airports to use construction materials that are made in the United States, often leading to higher costs and limited selection;
- The Davis–Bacon Act drives up the cost of labor by requiring contractors to pay workers arbitrary "prevailing wage" rates, which are 22 percent higher than market rates on average;[51] and
- Further regulations such as project labor agreements—which require contractors to use union labor—drive up the cost of construction.[52]

48. 49 U.S. Code § 47107.
49. Ibid.
50. Airport Innovation, Reform, and Reauthorization Act of 2016, H.R. 4441, 114th Congress, 2nd Sess., 2016.
51. James Sherk, "Why the Davis–Bacon Act Should Be Repealed," Heritage Foundation *WebMemo* No. 3451, January 12, 2012, http://www.heritage.org/research/reports/2012/01/why-the-davis-bacon-act-should-be-repealed.
52. David G. Tuerck, Sarah Glassman, and Paul Bachman, "Project Labor Agreements on Federal Construction Projects: A Costly Solution in Search of a Problem," Beacon Hill Institute *Policy Study*, August 2009, http://www.beaconhill.org/BHIStudies/PLA2009/PLAFinal090923.pdf (accessed November 3, 2016).

These costly regulations divert passenger tax revenues to favored special interests at the expense of much-needed airport improvements.

The cumulative burden of federal micromanagement has long hampered the airport industry. As long ago as 1987, a majority of large, medium, and small hub operators said they would forgo all federal grant assistance in return for the elimination of the federal regulations governing their operations and the ability to set their own airport user fees.[53]

Inhibition of Airports' Ability to Foster Air Carrier Competition and Develop Innovative Business Practices. The rules governing current sources of funding do little to empower airports to make improvements that could increase air carrier competition and yield benefits for travelers, such as building new terminals with increased gate access. Incumbent airlines with established gates at an airport have an incentive to maximize their market share at that airport. Because airlines are able to negotiate how their fees and capital investment are used in contractual agreements, they are unlikely to support the use of their revenues or investment on the construction of new gates for the use of other airlines or shared use, which could threaten their market share.[54] As a result, many gates at airports are exclusively or preferentially reserved for incumbent carriers, making it hard for new entrants to gain a foothold. This lack of air carrier competition is costly for passengers. A 2008 study from the Brookings Institution found that passengers paid $4.4 billion in higher fares (in 2005 dollars, roughly $5.4 billion in 2016 dollars) because of limited gate competition.[55]

Other funding options help perpetuate this entrenched system. AIP grants can be used only to cover the airside cost of new terminals, making them an unattractive tool for airports seeking to expand gate access for customers. Although the PFC has helped to provide a source for such improvements, the restrictions on these sources of funding inhibit airports from promoting pro-consumer development that could be promulgated under less restrictive conditions.

In addition, business practices that could help consumers are prohibited by limitations on airport revenue. Innovative pricing schemes and partnerships are likewise micromanaged by the FAA. For example, airports are unable to provide cash incentives to airlines to establish a new route to or from the airport, thus eliminating the opportunity for airports and airline to temporarily split the cost of the risk associated with establishing a novel route. The inflexibility of this regulation is fairly arbitrary, considering that the FAA allows airports to use temporary landing fee discounts as incentives for new entrants.[56]

FAA grant assurances also prohibit airports from using revenues for destination and tourist marketing, which could help foster competition between airports themselves and allow them to reach more potential customers. For example, under the current regulations, Orlando International Airport cannot spend revenues on advertising local attractions, but only on marketing the airport. As very few people take trips just to see the airport at their destination, this restriction is nonsensical. Creating the flexibility for airports to act like competitive businesses would encourage innovation and create more competition to the benefit of travelers.

Barriers to Privatization. The federal government's heavy-handed role has proved a major impediment to airport privatization, which would increase efficiency and improve management. Virtually none of the U.S.'s major commercial airports are privately owned.[57] This stands in stark contrast

53. Ronald D. Utt and Wendell Cox, "How to Close down the Department of Transportation," Heritage Foundation *Backgrounder* No. 1048, August 17, 1995, http://www.heritage.org/research/reports/1995/08/bg1048nbsp-how-to-close-down-the-department.

54. Other concrete examples of airlines seeking to maximize their market share at airports can be seen at airports where a limited number of takeoff and landing spots are controlled by the FAA. The most recent instance was the Justice Department filing suit to stop United Airlines from acquiring 24 additional slots at Newark Airport even though it already owned 902 (73 percent) of the slots and was not using 82 of them. While this is a separate issue from airport funding, it demonstrates that airlines have an incentive and multiple tools to maximize their market share at individual airports. See Robert Poole, *Airport Policy News*, Issue 112, Reason Foundation, June 2016, http://reason.org/news/show/airport-policy-security-news-112 (accessed November 3, 2016).

55. Steven A. Morrison and Clifford Winston, "Delayed! U.S. Aviation Infrastructure Policy at a Crossroads," The Brookings Institution, 2008, http://www.brookings.edu/~/media/research/files/articles/2008/5/aviation-winston/winston_aviation_chpt2.pdf (accessed November 3, 2016).

56. U.S. Department of Transportation, Federal Aviation Administration, *Air Carrier Incentive Program Guidebook*, September 2010, http://www.faa.gov/airports/airport_compliance/media/air-carrier-incentive-2010.pdf (accessed November 3, 2016).

to Europe, where 41 percent of airports are partially or wholly owned by private stakeholders. More importantly, the vast majority—73.5 percent—of passenger traffic in Europe is handled by private or partially privately owned airports. This share is rapidly increasing: In 2010, private or partially private airports accounted for 48 percent of traffic, indicating a 25 percentage point increase in just six years.[58] Similarly, Canada's airports were largely transferred to nonprofit corporations in the 1990s.[59] These figures indicate that the U.S. has a great deal of catching up to do in terms of allowing more efficient management of the nation's most important airports for the benefit of travelers.

European and Canadian airports are allowed to charge per passenger fees under a much less restrictive framework than the current PFC regime in the U.S. These fees make up a substantial portion of airport revenues for the largest European airports. A 2008 study conducted for the Dutch government found that per passenger charges made up 25 percent to 57 percent of revenues for nine major European airports.[60]

Unlike in Europe, investing in a private airport in the U.S. may seem unattractive because of the restrictions on revenue collection. Under the current PFC cap, airport administrators and private parties interested in airport ownership correctly question whether many airports could generate enough revenues to be self-sustaining and fund needed improvements. The impact of these restrictions was evidenced in Chicago Midway Airport giving up its bid for privatization when investors became concerned that the decreasing purchasing power of the PFC would not be adequate to fund their planned improvements.[61]

Furthermore, the federal government's involvement in regulating the ways in which airports can charge and use their revenues acts as a direct disincentive for private businesses to acquire or build commercial airports. A large regulatory barrier to brokering the sale of an airport is the way the grant assurances treat revenue diversions. Under a strict interpretation of the revenue diversion provision, an airport sponsor (e.g., a municipality or county) would be prohibited from spending any proceeds from the sale of an airport on non-airport-related expenses. Because most sponsors would no longer have any airports to operate and maintain following the sale of its airport, such a provision makes privatization financially pointless for the public entity involved.

Another disadvantage comes from the "exclusive use" and economic non-discrimination grant assurances, which limit airports' abilities to experiment with pricing and business models. The limitation on business models through federal restrictions may decrease investors' interest in financing an airport given the lack of flexibility and labyrinth of red tape that must be complied with simply to operate. Being unable to set and charge market prices, private entities face a huge disincentive to entering the airport market.

These disadvantages come on top of a financing system that heavily benefits public airports, which can issue tax-exempt bonds. A privately owned airport, on the other hand, cannot issue tax-exempt bonds, which means its borrowing would generally be more expensive than that of a publicly owned airport. Because the issuance of Private Activity Bonds (PABs) requires government ownership for airports, a private entity would instead need to lease the air-

57. The Luis Muñoz Marín International Airport, in San Juan, Puerto Rico, is the only commercial airport to be under private ownership via a long-term lease. Elias and Yang, "Issues in the Reauthorization of the Federal Aviation Administration (FAA)."

58. Airports Council International (Europe), *The Ownership of Europe's Airports, 2016*, March 8, 2016, https://www.aci-europe.org/component/downloads/downloads/4538.html (accessed November 10, 2016).

59. Rachel Yang, "Airport Privatization: Issues and Options for Congress," Congressional Research Service *Report For Congress*, No. 43545, February 3, 2016, https://www.fas.org/sgp/crs/misc/R43545.pdf (accessed November 3, 2016).

60. The airports examined include: Amsterdam Schiphol; Brussels; Paris-Charles de Gaulle; Frankfurt; London Gatwick; London Heathrow; Madrid Barajas; Munich; and Zürich. Joost Zuidberg and Jan Veldhuis, "Benchmark for Airport Charges and Governmental Taxes," SEO Economic Research, May 2008, http://www.seo.nl/uploads/media/2008-24_Benchmark_for_airport_charges_and_governmental_taxes.pdf (accessed November 3, 2016).

61. Marc Scribner, "The Conservative Case for a Modernized Passenger Facility Charge," *The Hill*, June 15, 2015, http://thehill.com/blogs/congress-blog/economy-budget/244878-the-conservative-case-for-a-modernized-passenger-facility (accessed November 3, 2016).

port from a government entity in order to qualify for tax-exempt qualified PABs. Even then, PABs are not as tax-advantageous as municipal bonds because interest generated by the latter is exempt from the Alternative Minimum Tax while interest from the Private Activity Bonds is not.[62]

To its credit, Congress recognized these barriers and established the Airport Privatization Pilot Program (APPP) in 1996 that waives certain regulations, including the revenue diversion issue at the point of sale.[63] However, the program has been drastically underutilized. Not a single major airport in the continental U.S. has successfully completed privatization through the program. The Luis Muñoz Marín International Airport, a medium hub airport in San Juan, Puerto Rico, is the only airport that has successfully completed privatization through the APPP.[64] Although changes to the program could help spur its use, the industry's tepid response suggests that greater regulatory and policy changes may be needed in order to bring about large-scale privatization efforts like those in Canada and Europe.

Towards Free-Market Airports: Ending Federal Involvement in the Airport Business

The FAA states that the nation's airports "should be affordable to both users and the Government, relying primarily on producing self-sustaining revenue and placing minimal burden on the general revenues of the local, State, and Federal Governments."[65] Yet the barriers established by the federal government's management of airport funding have been a direct barrier to the goal of self-sustainability and have not allowed American airports to reach their full potential in terms of modernization, capacity expansion, and greater competition. While there is room for both the federal government and airports to yield improvement through tweaking the current system, the best way to revitalize the nation's airports would be to gut the current middle-man funding scheme and embrace a free-market arrangement for airports. To accomplish this goal, the following steps should be taken:

1. Repeal the Anti-Head Tax Act. Congress should repeal the Anti-Head Tax Act.[66] This would enable airports to levy fees on their customers for the services they provide, replacing the PFC program and the need for federal grants.

2. Eliminate Federal Airport Funding and Reduce Passenger Taxes. In conjunction with lifting the ban on local charges, Congress should phase out the AIP program and reduce aviation taxes correspondingly. This tax reduction would allow local fees to take the place of airport taxes and the subsequent grants they fund. The reduction in passenger taxes should be a first step in the ultimate elimination of passenger taxes, which could be realized following subsequent reforms such as the privatization of the Air Traffic Organization, which is also funded by passenger taxes.[67] Other funding programs and subsidies, like the Essential Air Service, should also be repealed. Ending the federal funding mechanism will ensure greater efficiency and end the cross-subsidies that occur between large and small airports, yielding savings and better service for the vast majority of fliers. Airports that currently rely on federal subsidies will need to charge users for the true cost of service or seek subsidies at a local level of government as a last resort if they are not commercially viable.

3. Reform Grant Assurances. Grant Assurances are the restrictive regulations governing how airports may operate if they receive Airport Improvement Grants. [68] Temporary Grant Assurances made on federally funded infrastructure and projects

62. Steven Maguire, "Private Activity Bonds: An Introduction," Congressional Research Service *Report for Congress* No. 31457, June 9, 2006, http://research.policyarchive.org/19149.pdf (accessed November 3, 2016).
63. Federal Aviation Reauthorization Act of 1996, Public Law 104–264, and Elias and Yang, "Issues in the Reauthorization of the Federal Aviation Administration (FAA)."
64. Ibid.
65. U.S. Department of Transportation, Federal Aviation Administration, *Report to Congress: National Plan of Integrated Airport Systems (NPIAS)*, 2016.
66. 49 U.S. Code § 40116 (b), et seq.
67. See Robert Poole, "The Urgent Need to Reform the FAA's Air Traffic Control System," Heritage Foundation *Backgrounder* No. 2007, February 20, 2007, http://www.heritage.org/research/reports/2007/02/the-urgent-need-to-reform-the-faas-air-traffic-control-system.
68. 49 U.S. Code § 47107.

currently underway using public funds should be waived or allowed to expire. Permanent Grant Assurances, including those regarding Airport Revenues (Assurance 25) and Exclusive Rights (Assurance 23), should be eliminated or made temporary and then allowed to expire. If waiving the assurances outright is impractical, then allowing the assurances to expire on an accelerated timeline should be considered.

4. Ensure Limited and Effective Oversight. Because almost all commercial airports are government-owned and many enjoy outsize market power in their areas, an oversight mechanism should exist to ensure these government monopolies do not abuse their market power or treat airport customers as a windfall for local government budgets.

For example, the Port Authority of New York and New Jersey—which manages John F. Kennedy, LaGuardia, and Newark airports, among others—is exempt from the revenue diversions grant assurance because it had a pre-existing agreement with the FAA and was exempted from the restrictions extended by the Airport and Airway Safety and Capacity Expansion Act.[69] This has allowed the Port Authority to divert airport funds to other money-losing Port Authority activities such as the Port Authority Trans-Hudson (PATH) commuter rail, the only commuter rail in the country that does not rely on local tax subsidies for operation. This cross-subsidy to non-airport activities has resulted in much complaining from airlines and travelers, who experience excessively high fees to buttress the Port Authority's unprofitable ventures. The Port Authority is able to maintain this practice because it is the monopoly owner of New York's major airports.[70] Although increased airport competition from new private airports would help ameliorate this problem, action may be needed to safeguard consumers from wide-scale government abuse such as that effected by the Port Authority.

The enabling legislation should continue to task the Transportation Secretary with the ability to mediate cost disputes between government-owned airports and other parties in the event that the Secretary deems that an airport fee is unreasonable. The Secretary is currently responsible for this oversight.[71] The Secretary's authority, however, should be confined to regulating the fees only if he finds both conditions to be true:

- A government-owned airport (or its sponsor) exercises an effective monopoly in the area in question.
- The charge levied by the airport is unduly burdensome on interstate commerce, consistent with the Supreme Court's ruling in *Evansville*. That is, if the charge in question is not "based on some fair approximation of use or privilege for use," or is "excessive in comparison with the governmental benefit conferred."

This will limit the Secretary's reach to cases in which a governmental entity has clearly abused its market power. Likewise, states and localities should remain prohibited from administering a sales tax or other levy on the fee simply to augment their budgets with new revenues.

Furthermore, care must be taken to uphold the spirit of the revenue diversion grant assurance to ensure that local governments do not use the airport's new self-derived revenues to pad local budgets or fund projects wholly unrelated to the airport.[72] One safeguard less restrictive than current practice would be to require that any use of revenue on off-airport causes (such as to pursue off-airport transit projects) gain the approval of a majority of the airport's airline tenants.

5. Allow Free-Market Airports to Flourish. Liberating airports from restrictive federal over-

69. U.S. Department of Transportation, Federal Aviation Administration, *Airport Compliance Manual*, Chapter 15.

70. Seth Barron, "The Port Authority Leviathan," *City Journal* (Winter 2016), http://www.city-journal.org/html/port-authority-leviathan-14172.html (accessed November 3, 2016), and Citizens Budget Commission, "Financing PATH: Options for Deficit Reduction," April 2014, http://www.cbcny.org/sites/default/files/REPORT_PATH_04242014.pdf (accessed November 3, 2016).

71. 49 U.S. Code § 47129.

72. Many local governments are increasingly experiencing budget constraints from growing retirement and pension costs. New options for revenue, such as those from airports, may be very attractive indeed to these governments. See, e.g., Stephen Eide, "California Crowd-Out: How Rising Retirement Benefit Costs Threaten Municipal Services," Manhattan Institute Report, April 16, 2015, https://www.manhattan-institute.org/html/california-crowd-out-5878.html (accessed November 3, 2016).

sight and funding mechanisms will localize airport funding and help reduce the barriers to privatizing airports. The revenue restrictions posed by regulations and strict grant assurances will no longer exist, which should increase airports' attractiveness and the likelihood that they can generate enough revenue to attract new management and spur the construction of new airports. Airports themselves will have an incentive to expand and increase competition among airlines at their facilities. Furthermore, the flexibility created by waiving grant assurances could allow airports to eschew traditional pricing models and experiment with new business arrangements, creating even more competition amongst airports themselves.

Invigorated air carrier and inter-airport competition in future markets will help protect consumers against excessive rent-seeking by government and private monopolies. In the event that competition does not provide an immediate remedy, privatized airports could be held to the same standards as administered by the Secretary above to ensure that a monopoly power does not encroach upon interstate commerce. Likewise, the FAA will continue to hold all airports to safety standards and requirements.

Options for Incremental Reform

Given the entrenchment of special interests and the tendency of Congress to legislate in favor of more government involvement in the economy (including the aviation sector), smaller reforms towards this free-market system may be necessary at first. Short of completely eliminating federal involvement in funding airports, Congress could consider:

- **Exempting** large and medium hubs from the Anti-Head Tax Act. If this exemption is not politically possible, Congress could alternatively increase or eliminate the federal cap on PFCs.
- **Reducing** substantially passenger taxes and reforming AIP eligibility to ensure that the major airports that can most benefit from airport fees or PFCs are no longer eligible for federal funding.

These two incremental reforms would provide an intermediary step towards a free-market system while allowing the most systemically important airports to move towards self-sufficiency and ultimately privatization.

Enable the Nation's Airports to Adapt to 21st-Century Aviation Needs

The nation's aviation system is vital to the U.S. economy and has experienced rapid growth since the 1980s, which is expected to be sustained in the near future. Yet as the industry's needs are anticipated to expand, the federal government continues to hold it back. Instead of continuing top-down, redistributive funding and heavy-handed regulation, the federal government should step back and allow the aviation system to flourish. Congress and the next President can accomplish this by:

- **Eliminating** burdensome regulations that restrict how airports can raise and spend revenues;
- **Reducing** costly passenger taxes and **eliminating** inefficient federal grants; and
- **Allowing** self-sufficiency and privatization to move U.S. airports towards a modernized, free-market funding system.

By bringing about funding autonomy and greater room for innovation, these reforms will help modernize the nation's airports to the benefit of all Americans.

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