STATEMENT OF MARION C. BLAKEY, ADMINISTRATOR OF THE FEDERAL AVIATION ADMINISTRATION, BEFORE THE SENATE COMMERCE, SCIENCE AND TRANSPORTATION COMMITTEE, SUBCOMMITTEE ON AVIATION, ON FAA'S FY2007 BUDGET AND THE VIABILITY OF THE AIRPORT AND AIRWAY TRUST FUND. MARCH 28, 2006.

Chairman Burns, Senator Rockefeller, Members of the Subcommittee:

I welcome the opportunity to be here today, along with my colleagues from the Inspector General's Office and the Government Accountability Office (GAO), to discuss the state of the Federal Aviation Administration's (FAA) financial health, specifically our budget for fiscal year 2007 and the condition of the Airport and Airway Trust Fund (AATF or Trust Fund). The financial health of the aviation trust fund is closely linked to the stability of the aviation industry. I understand that today's hearing will lay the foundation for a hearing in several weeks where future funding options for the FAA will be addressed in detail. I look forward to returning and discussing the specifics of the Administration's proposal.

First let me briefly express appreciation for the dialogue that has begun with our stakeholder community. Over the past year, under Secretary Mineta's leadership, we have conducted a broad outreach to the aviation community to explore funding options that would be in the long-term best interest of the traveling public, the aviation industry and the FAA. We held a public forum last April and have conducted numerous group and individual briefings with our stakeholders. To inform the dialogue we published detailed industry activity data as well as a set of principles which we thought should underlie and guide the discussion. In my view the thoughtful comments we have received have greatly informed our decision making. We at the FAA have listened intently and have benefited from a wide range of expert views.

As I've often stated over the past year during our outreach, our belief in the need for funding reform for the FAA is not fundamentally about generating more money for the FAA. It is about creating a more rational, equitable and stable system that provides appropriate incentives to users and to the FAA to operate more efficiently and facilitates modernization of the aviation system on an assured and predictable basis.

Fiscal Year 2007 Budget Proposal

I would like to address the FAA's budget in the near term. As you know, the FAA operates 24 hours a day, 7 days a week, 365 days a year. We run a multi-billion dollar air traffic control system that in FY 2005 served 739 million passengers and over 39 billion cargo revenue ton miles of freight. We operate and maintain a system comprised of more than 70,000 facilities and pieces of equipment. There are FAA-operated or contract towers at 500 airports, and we are also responsible for inspection and certification of about 220,000 aircraft and 610,000 pilots. We have some 43,000 dedicated government employees working to serve the traveling public and the businesses that depend on the air transportation system.

When Congress mandated the FAA to realign our operations and manage more like a business, we rose to the challenge. The FAA's efforts over the past three years have paid real dividends, not just to the flying public but to the taxpayer as well. By implementing improved management tools, including better cost-accounting systems and instituting a pay-for-performance program, we have been able to make better use of our resources. The tangible results are reflected in our FY 2007 budget request of $13.7 billion. The request upholds our commitments to increase the safety, capacity, and efficiency of the national aviation system.

The FY 2007 budget provides $8.4 billion for our Operations account and reflects the rising labor costs and challenges the FAA faces. This year, we completed the largest A-76 competition in government and will see the first installment of cost savings --$66 million-- in FY 2007. This contract not only saves money; it also commits the vendor to modernize and improve the flight services we provide to general aviation pilots. The agency's emphasis on bottom-line results has not been easy. The FAA has slashed costs where possible and slowed the rate of growth of our labor costs through productivity improvements. We also continue to apply effective management and financial principles to our labor negotiations. The simple fact of the matter is that we cannot and will not sign a contract that the taxpayer cannot afford. Since 1998, the first year of the current NATCA contract, the increasing imbalance in compensation between NATCA and the rest of the agency has cost the taxpayer $1.8 billion. Neither the FAA nor the taxpayer can afford a repeat performance. As a result, future labor agreements will be fair, affordable and protect management's rights. We have been negotiating with NATCA for more than eight months, and I am hopeful that we will be able to reach a voluntary agreement, particularly now that both sides have been working with the help of a federal mediator during the last few weeks. Both sides recently agreed to a short extension of the mediation, and I anticipate this will come to closure shortly, hopefully by a voluntary deal.

Long-term affordable pay structures are only a part of the equation. In addition, we are taking steps to achieve savings of 10 percent by FY 2010 in controller staff costs through productivity improvements. We achieved the first 3 percent of this goal in FY 2005 and, overall we avoided approximately $23 million in costs last year. This fiscal year and in FY 2007, we project a minimum of a 2 percent productivity improvement each year.

We expect a continuous wave of controller retirements over the next 10 years, as 72 percent of our air traffic controllers become eligible to retire. Bringing aboard new controllers is a complex process and it takes several years to train a controller. Our budget request supports our hiring needs for both air traffic controllers and safety inspectors.

For Facilities and Equipment (F&E), we are requesting $2.5 billion to improve and modernize the airspace system. We are also scrutinizing our capital investments; revisiting business cases and weeding out programs whose benefits no longer justify the costs; and we are increasing our emphasis on programs that will save the agency money.

We are making similar inroads with equipment. In FY 2005, we removed 177 navigation aids from service, which saved the taxpayer about $2.7 million. This year, we plan to remove 100 more, followed by another 100 in 2007. We are taking steps to save wherever possible. In fact, our five-year strategic plan, the FAA *Flight Plan*, sets cost savings and productivity improvement goals for all organizations in the agency.

Our resources and activities are closely linked with the dynamic industry we oversee and serve. The pace and depth of change in aviation is unparalleled. Business models evolve as rapidly as the technology changes: markets once dominated by wide body aircraft are now giving way to smaller jets. Entrepreneurs now are marketing microjets, which may one day become the “personal taxi” of the sky. Fractional ownership is making it easier for businesses to own and operate aircraft.

Even with the financial shake-up in the airline industry, all major forecasts project that the demand for air travel will outstrip existing capacity. After a very slight decline in projected operations at airports with FAA or contract towers, we forecast an average annual growth of two percent and forecast a three percent annual growth for en route operations (from 2005-2017). Air travel now exceeds pre-September 11 levels and remains on track to carry more than 1 billion passengers by FY 2015.

The future portends a wide range of aircraft with divergent infrastructure, air traffic management, regulatory, and procedural requirements. We must be prepared to support a system that includes the A380 and the microjet (and everything in between). We must be able to support airlines, large and small, national and regional. Recognizing that aviation represents about nine percent of the America’s Gross Domestic Product, we must provide this infrastructure in time to keep the U.S. economy growing while controlling the costs of that system.

<u>Safety</u>

Safety remains our number one priority and our number one success story, with the trends in both commercial and general aviation showing consistent improvement. The safety record we have achieved for air carriers is a remarkable accomplishment, which our entire workforce—inspectors, engineers, technicians, and controllers—shares with the broad aviation community. Over the past four years, 3 billion people have traveled safely in the air transportation system---that's ten times the population of the U.S.

The FY 2007 budget reflects the agency's steadfast commitment to safety. Out of a total request of $13.7 billion, about 70 percent, or $9.6 billion, will contribute to our efforts to improve our already historic safety record. This includes further progress in reducing commercial and general aviation fatality accidents, the numbers of runway incursions, and HAZMAT incidents. Our overarching goal is to measure and achieve the lowest possible accident rate, while constantly improving safety.

Grants-in-Aid to Airports

In today's challenging budget environment, we have been forced to take a long hard look at our funding requirements. Our FY 2007 budget request for Grants-in-Aid to Airports is $2.75 billion which is lower than recent authorized and enacted levels. Nevertheless, under our proposed budget, FAA will be able to support all high priority safety, capacity, security and environmental projects. There will be adequate funds to meet all current and anticipated Letter of Intent (LOI) commitments, which relate to high priority, multi-year projects within the national system. The President's Budget includes support of major capacity projects such as the Chicago O'Hare redesign, new runway at Washington Dulles International Airport and major projects at Atlanta-Hartsfield International. We will also be able to fund projects to meet the FAA's Flight Plan goal for improving runway safety areas (RSAs), help airports meet their Part 1542 security requirements, and continue work on phased projects.

Technology for the future

We are laying the foundation for our future with a commitment to increasing the system's capacity to accommodate the air transportation system's predicted growth. We will meet these future needs by harvesting new technologies that will support the Integrated

National Plan for the Next Generation Air Transportation System (NGATS). This Plan, submitted to Congress in December 2004, brings together six cabinet-level groups in the Joint Planning and Development Office (JPDO) to eliminate duplication and wasted resources. The Plan is a roadmap that will leverage federal funds and allow us to provide the national aviation system that can handle the safety, capacity and security needs of the future.

For the FAA, the Plan has already been integrated into our budget. Our 2007 budget begins to build this new infrastructure by, for example, supporting two promising technologies: Automatic Dependent Surveillance – Broadcast (ADS-B) and System Wide Information Management (SWIM). The capabilities of ADS-B are already proven in the field. ADS-B provides: (1) automatic broadcast of aircraft position, altitude, velocity, and other data; (2) enhanced "visibility" of aircraft and vehicle traffic for pilots and air traffic controllers; and (3) use of Global Positioning Systems, allowing us to reduce our reliance on ground-based infrastructure. SWIM makes advanced information distribution and sharing capabilities possible. Every year, FAA builds applications for air traffic management systems that require unique interfaces between the new application and existing systems. SWIM will replace those unique interfaces with a reusable interface and provides many operational benefits.

The above overview of our FY 2007 budget is how we propose to meet the challenges over the near term for the FAA, and also provide for the long-term with our Integrated National Plan for NGATS. At the same time, we are also planning for the next reauthorization of our programs and how those programs will be funded. Critical to that endeavor is an examination of the status and outlook of the Airport and Airway Trust Fund and what that means for the FAA's long term financial picture.

The Airport and Airway Trust Fund

The Airport and Airway Trust Fund was created in 1970 to provide a dedicated source of funding for the aviation system. Before there was a Trust Fund, a 5% tax on passenger airline tickets, a general aviation fuel tax, and a tire and tube tax were deposited in the General Fund. Today Trust Fund revenues are generated by a combination of taxes that were last authorized in 1997: a domestic passenger ticket tax of 7.5% of the price of a ticket, a domestic flight segment tax of $3.30 per segment per passenger, an international departure/arrival tax of $14.50 per international passenger, an Alaska/Hawaii departure tax of $7.30 per passenger traveling between these states and the continental U.S., a 6.25% waybill tax on domestic cargo and mail, a general aviation (GA) jet fuel tax of 21.8 cents per gallon, a GA aviation gasoline tax of 19.3 cents per gallon, and a commercial fuel tax of 4.3 cents per gallon. The domestic segment tax, international departure/arrival tax, and Alaska/Hawaii tax rates are indexed to the Consumer Price Index and have increased each year for the last four years, but the airline ticket tax is a fixed percentage of the ticket price, so it is dependent on changes in airline ticket prices rather than general inflation. These taxes and fees are scheduled to expire in September 2007, which also coincides with the end of the current authorization for FAA programs under Vision 100.

Each year, the FAA is funded by annual appropriations drawn both from the aviation Trust Fund and from the General Fund. There has been a long history of funding a portion of the FAA's operating costs out of the General Fund due to recognition that aviation provides benefits to the non-traveling public and to our economy as a whole. However, the ratio of General Fund versus aviation Trust Fund financing has varied over the years. The General Fund share of total FAA appropriations has been as high as 59 percent (in FY 1984) and as low as zero (in FY 2000). The trend, however, is not in question. On average over the last 15 years, the portion of operating costs coming from the General Fund has declined steadily. In FY 2005, about 20 percent of the FAA's total budget came from the General Fund and 80 percent from the Trust Fund; this year it's 18 percent and 82 percent, respectively.

In recent years, appropriations from the Trust Fund have been funded not only from the annual revenue going into the fund and interest posted to the Trust Fund, but also from drawing down the AATF's balance, which was over $7 billion as recently as 2001. A gap exists when you compare the revenue going into the Trust Fund with the level of our costs, and this gap is quickly eroding the Trust Fund. Since the start of FY02, the uncommitted balance* of the Trust Fund has declined by more than $5.4 billion, or an average of 28% per year. When there is no relationship between the level of revenue being raised to the costs being funded from the Trust Fund, factors such as fluctuating ticket prices that do not raise enough revenue, volatile demand so there are fewer passengers paying for travel, and fundamental changes in the airline industry such as the decreasing size of aircraft being used for commercial transport, lead to a revenue shortfall that has been funded by drawing down the Trust Fund balance. With the increasing pressures on the budget to fund military and national security needs, the Trust Fund remains a critical necessity in closing the funding gap. Last year (FY05), the uncommitted balance at the end of the fiscal year was $1.9 billion and, this fiscal year, the President's budget projects that it will dip to approximately $1.7 billion at the end of the fiscal year.

The FY2006 projected level of the uncommitted balance is sobering because it leaves only a small "cushion" in the Trust Fund balance. In addition, our ability to rely on an increased General Fund contribution to bridge any gap is in question due to competing budget pressures as well as the effort to reduce the federal deficit.

As we look to the future, we see a complicated air traffic control system and workload. As noted above, scheduled commercial passenger demand, which dipped severely in the wake of 9/11, exceeded pre-9/11 levels last year reaching a record 739 million passengers, up from 690 million in FY 2004. We expect that domestic passenger totals

* The uncommitted balance consists of surplus revenues in the Trust Fund against which no commitments, in the form of budget authority, have been made. This measure provides the most widely-accepted estimates of the amount of money available in the Trust Fund for new appropriations for aviation purposes.
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will continue to grow at approximately three percent per year with the international sector growing five percent per year.

Low-cost carriers and regional carriers (using smaller jets) are continuing to redefine the market. Revenue passenger miles(RPM) for the regional carriers are expected to grow almost seven percent per year, and we forecast annual RPM growth of almost eight percent for low-cost carriers. We forecast that regional carriers will increase their share of the U.S. domestic market from 22 percent last year to more than 25 percent by 2017. In FY 2005, commercial activity at 23 of our 35 major airports exceeded FY 2000 (peak) activity levels. Las Vegas (37%); Ft. Lauderdale (33%); Salt Lake City (30%); and Minneapolis (30%) experienced the greatest increases in operations.

It is of course very good news for the aviation industry that demand is back, but it is back in different ways than before. While low fares are good news for the passenger, they spell trouble for the Trust Fund with its heavy reliance on the ticket tax as its primary source of revenue. Approximately 50% of the Trust Fund revenue currently comes from the 7.5% tax on domestic airline tickets.

Industry changes also have implications for the FAA's workload. The airlines are trying to control costs by using increasing numbers of smaller aircraft. This trend adds to the workload of air traffic controllers without increasing tax revenue commensurately. Regional jets normally carry fewer passengers than the larger airliners, so the movement toward smaller passenger aircraft contributes to the decline in the Trust Fund revenue per flight. If an airline carries a given number of passengers (paying the same fares) on two regional jets instead of one larger jet, ticket tax revenue does not change, but controller workload approximately doubles. Our latest forecasts indicate that the growth in the number of smaller aircraft is expected to continue, driving down the average number of seats of a domestic aircraft through 2011. Plainly, our revenue is not tied to the cost of the service, which means that there is no nexus between actual workload and how it's paid for.

Increased air traffic operations are not the only source of increased workload for the FAA. In recent years the industry has also seen more new entrant carriers. While this is good news for competition, it also has workload implications for our agency. Right now, there are 10 applications in the queue awaiting review and certification by our safety staff, and each of these new operators will bring additional pilots and crew into the system. Also, with regard to our airport grant program, Vision 100's increase in funding for the Airport Improvement Program (AIP) coupled with a new entitlement formula apportionment for non-primary airports increased our workload in processing grant applications by fifty percent.

Knowing what is happening with Trust Fund revenues and how the changes in the aviation industry affect our workload is only part of the equation. We know we must also continually work very hard to control our costs--to make changes and become more efficient, more business like. We are changing the agency's structure with a major shift to a performance-based organization, and, as I noted above in discussing our budget proposal, making tough choices with our funding. We have implemented a cost accounting system in the ATO that provides our managers and executives with the information they need to identify and eliminate wasteful spending, hold or reduce operating costs, and better link financial performance to mission objectives. That cost accounting system is being extended throughout the FAA this year to help us better assess and control our costs.

I've already mentioned our cost savings measures by the ATO, our challenges with our labor negotiations and with future controller hiring. We are also faced with an aging and deteriorating inventory of facilities and equipment. The average condition of the FAA's 21 en route air traffic control centers is poor and getting worse each year. As this Committee well knows, modernization of the air traffic control system is critical if the agency is to keep up with what aviation brings tomorrow. The price tag for these facilities and equipment alone is $2 billion per year in capital funds just to maintain current services.

In addition to maintaining the current infrastructure, the JPDO is planning for the emergence of the next generation of the air transportation system out to 2025, charting the course for satellite based navigation, handling new aircraft classes, on-demand services, and the increasing growth in air traffic. However, the move to a modern, efficient and technology-driven aviation system is going to require sustained, multi-year investments. We will need to invest resources in order to make the transition to a new system that will significantly reduce operating costs and better serve our customers in the long run.

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

Tying funding to the cost of providing service protects both FAA and the customers who use FAA services by not subjecting our ability to provide a certain level of service to unrelated factors like ticket prices. A stable, cost-based revenue stream can also ensure funding for long-term capital needs. We also believe that a cost-based revenue structure would provide incentives to our customers to use limited resources efficiently and to the FAA to operate efficiently, as stakeholder involvement can help us ensure that we are concentrating on services that the customer wants and is willing to pay for.

Conclusion

We believe that the revenue stream that currently funds the FAA is not tied to the cost of the services and that there is a need for funding reform. FAA's workload continues to increase. The current system, largely based on the ticket tax, provides no nexus between the actual workload of controlling flights and providing other services and how they are paid for. It is time for change.

Mr. Chairman, ten years after the NCARC recommendations, we are tackling probably the hardest part of reform: how the aviation transportation system will be financed in the next decade and beyond. Our proposal for funding reform for the FAA is now under review within the Administration. As I noted at the outset, it is the product of extensive public outreach, analysis, and a lot of creative thinking. It will propose a cost-based funding structure which will ensure that our costs and revenues are aligned and that our stakeholders are treated equitably. The details will come soon in the form of a legislative proposal, which I hope will be the basis for ongoing dialogue with this Committee and others in Congress, our colleagues in the aviation community, and the public.

I look forward to the debate and expect that the discussions will be frank, open and spirited. We have an opportunity in the near future for positive change, to correct the faults of the current system that threaten our ability to meet future demand. Change is always unsettling and difficult and requires patience and hard work, but to be ready for tomorrow we must begin today. It is the only way that we will be able to continue to operate and maintain the world's safest system with the capacity our economy needs.

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