

**AIR SERVICE IN THE UNITED STATES:
FEDERAL GOVERNMENT ASSISTANCE TO COMMUNITIES**

Allison Padova
Economics Division

24 October 2003

The Parliamentary Research Branch of the Library of Parliament works exclusively for Parliament, conducting research and providing information for Committees and Members of the Senate and the House of Commons. This service is extended without partisan bias in such forms as Reports, Background Papers and Issue Reviews. Analysts in the Branch are also available for personal consultation in their respective fields of expertise.

**CE DOCUMENT EST AUSSI
PUBLIÉ EN FRANÇAIS**

TABLE OF CONTENTS

	Page
INTRODUCTION	1
ESSENTIAL AIR SERVICE PROGRAM.....	1
A. History.....	1
B. Eligibility	2
C. Administration	3
D. Funding	5
E. Outlook	7
SMALL COMMUNITY AIR SERVICE DEVELOPMENT PILOT PROGRAM.....	8
A. History.....	8
B. Eligibility	9
C. Administration	10
D. Funding	11
E. Outlook	11



CANADA

LIBRARY OF PARLIAMENT
BIBLIOTHÈQUE DU PARLEMENT

AIR SERVICE IN THE UNITED STATES: FEDERAL GOVERNMENT ASSISTANCE TO COMMUNITIES

INTRODUCTION

The United States considers that some level of air service to small and medium-sized communities is vital to their economic growth and diversity. In some cases, it may also be the community's only means of access for part or all of the year. To this end, the United States has developed two federal programs to ensure that communities get the air service they require. Under the first of these programs, small and/or remote communities that might otherwise be left without air service as a result of airline deregulation are eligible for subsidized air service. More recently, a pilot program was introduced to assist small and medium-sized communities that have inadequate air service or excessive airfares, by providing financial assistance for programs that could improve their situation in either regard. This paper provides information on both programs in terms of eligibility, administration and funding arrangements, as well as their future outlook.

ESSENTIAL AIR SERVICE PROGRAM

A. History

The United States legislated a subsidy program at the time of airline deregulation in 1978, anticipating that air carriers would shift operations from small communities, where service was unprofitable, to larger, more lucrative markets. Section 419 of the Federal Aviation Act established the essential air service (EAS) program, which is administered by the Department of Transportation (DOT). The program's purpose was to ensure that smaller communities that had air service prior to deregulation would remain linked, with a federal subsidy if necessary, to the national air transportation system.

The EAS program was initially authorized for only 10 years, through 1988, during which time the impact of deregulation on affected communities would be phased in. Small carriers were expected to emerge in the deregulated environment and find some of these small markets viable. Where this did not happen, the 10 years would be a grace period for communities to adjust to the prospect of losing service altogether when the subsidies were eliminated. Before this could happen, the Airport and Airway Safety and Capacity Expansion Act of 1987 extended the program for another 10 years and specified a sunset date of 30 September 1998. Finally, in 1998 the Rural Air Service Survival Act rescinded the sunset date and established a permanent funding authorization for the program. The reason for the program's continuation may have been that it reportedly had significant support in the Senate, where rural states have a stronger voice than in the House of Representatives.⁽¹⁾

B. Eligibility

All small communities listed on air carrier operating certificates and receiving service at the time of deregulation are eligible for the regular EAS program. In 1978, 383 communities were participating in the EAS program out of nearly 800 listed on air carrier certificates.⁽²⁾ Congressional appropriations for the program in the late 1980s and the early to mid-1990s were insufficient to meet demand, leading to funding shortfalls and the abandoning of service to many communities, at least temporarily. As well, more than 50 communities have been permanently eliminated from the program due to the introduction of additional eligibility criteria.

To be eligible for the program today, a community that received air service at the time of deregulation must be more than 70 highway miles from a medium or large hub airport. Per-passenger subsidies for communities fewer than 210 miles from such an airport are capped at \$200. Thus, if a carrier requires an operating subsidy that works out to more than \$200 per passenger carried in the previous year, the service is not commissioned.

Communities listed on air carrier certificates that did not receive air service at the time of deregulation can also participate in the EAS program, subject to the same eligibility requirements. They are not considered part of the "regular" program, however, and are required to pay 25% of the subsidy required to secure basic air service.

(1) Two senators represent each state in the Senate, whereas the number of congressmen for each state in the House of Representatives is relative to population.

(2) Not all of the communities in the program require a subsidy to maintain air service.

New communities can join the program if they are willing to contribute 50% of the subsidy required. In order to join, the community must make a proposal to the Secretary of Transport showing potential for traffic generation, distance from the nearest hub and some estimate of the subsidy required to obtain air service.

C. Administration

Communities that are eligible for the regular EAS program can expect the DOT to ensure that “basic air service” to their community is maintained. Since the Airport and Airway Safety and Capacity Expansion Act of 1987, basic air service is characterized as follows:

- service to a hub (medium or large) airport;
- no more than one intermediate stop;
- service with aircraft having at least 15 seats at communities that average more than 11 passenger enplanements per day;
- service with pressurized aircraft under certain circumstances; and
- schedules that consider the needs of passengers with connecting flights.

The Department determines which hub will be used, as well as the minimum number of round trips and available seats. The subsidy to be paid amounts to the carrier’s prospective operating loss plus a profit margin. Competitive pressure on air carriers, generated by the bidding process, is expected to ensure that cost estimates are reasonable.

The community may negotiate with an air carrier to provide the service or request the DOT to solicit proposals on its behalf. Proposals are evaluated on a number of technical criteria; the DOT also considers community preferences. Contracts for air service are usually for two years, at which time the DOT either negotiates continuation of the service or solicits proposals again. If a carrier wishes to terminate service, it must provide 90 days’ notice to the community, the State agency and the DOT. If a non-subsidized carrier wishes to replace the incumbent before the end of the notice period, it may do so if it offers a reasonable level of service and the DOT deems the carrier to be fit.

In 2003, the EAS program funded air service to approximately 130 communities in the United States and carried about one million enplaned/deplaned passengers.⁽³⁾ Nearly all of the

(3) Each enplaned/deplaned passenger represents one round-trip traveller. One million enplaned/deplaned passengers represent less than one-fifth of one percent of the total domestic air travel market in the United States.

Alaskan communities that receive subsidized service have no access to the road system.⁽⁴⁾ Similarly, some communities served in Hawaii depend on air service for food, mail, access to hospitals and basic supplies. Subsidies per route as of June 2003 ranged from just under US\$300,000 to just under US\$2.5 million per annum.⁽⁵⁾ The average annual subsidy per route is nearly US\$900,000. The administration of the EAS program, which is undertaken by approximately six full-time DOT employees, is summarized in Table 1.

Table 1: EAS Program – Administration

Step	Details
Eligibility	<p>Eligible communities include:</p> <ul style="list-style-type: none"> • Communities listed on air carrier certificates in 1978 that received service; • Communities listed on air carrier certificates in 1978 that did not receive service (subject to 25% cost sharing); and • New communities (subject to 50% cost sharing) <p>Subject to:</p> <ul style="list-style-type: none"> • 70-mile minimum distance from nearest medium or large hub airport, and • \$200 maximum per-passenger subsidy if within 210 miles of hub
Contract with air carrier	Community may negotiate with carrier or request Department to solicit proposals on its behalf. Department's decision considers community preferences and a number of technical criteria.
Period of contract	<p>Normally two years.</p> <p>At the end of the period, the Department will either negotiate continuation of service or solicit proposals again.</p> <p>Subsidy covers carrier's prospective operating loss plus a profit margin.</p>
To terminate, suspend or reduce service	<p>90-day notice to community, State agency and Department is required.</p> <p>Non-subsidized carrier may replace incumbent before end of notice period if the proposed service is reasonable and the carrier is deemed fit.</p>

(4) Over 30 communities in Alaska receive subsidies from the EAS program.

(5) Note that some communities receive subsidized services on more than one route.

D. Funding

Program appropriations averaged US\$74 million per annum in its first four years, funding an average of 375 communities. Appropriations between 1986 and 1997 were significantly lower, averaging US\$30 million per annum. During this period, the average number of communities funded by the EAS program was about one-third that of the first four years. Thus, while the average cost of the program per community was rising, the number of communities benefiting from the program was falling.

In 1998, the Rural Air Service Survival Act (part of the Federal Aviation Administration Reauthorization Act of 1996) established a permanent authorization of US\$50 million for the program. Congress appropriated the full amount authorized by the Act of 1998 until 2002, at which time additional amounts were appropriated. The EAS program received the highest level of funding in its history in the 2002 and 2003 fiscal years to offset the negative impact of the terrorist attacks of September 11, 2001, on the air transport industry.⁽⁶⁾ The appropriation in 2004 is expected to fall back to US\$50 million. EAS program appropriations since its first year are shown in Table 2.

Prior to 1992, the EAS program was financed from general revenues. Since 1992, the Federal Aviation Administration's (FAA) Airport and Airway Trust Fund has financed the cost of subsidizing the provision of essential air service.⁽⁷⁾ The trust fund consists of tax revenues received from the commercial transportation of persons and property by air, sales of gasoline and jet fuel used in commercial and non-commercial aircraft, and an international departure tax. The Rural Air Service Survival Act of 1998 specified that the US\$50 million per annum it authorized for the program should come from overflight fees collected by the FAA from aircraft that neither take off nor land in the United States. The courts have struck down this proposal every year, and the program continues to be funded by the FAA's Airport and Airway Trust Fund.

(6) As a result of the September 11 attacks, the costs of insurance and security increased air carriers' costs. More importantly, however, passenger traffic fell off and carriers serving EAS communities were unable to generate the expected amount of passenger revenues. Under these new conditions, the federal government had to step in with increased funding to maintain the promised level of service to eligible communities.

(7) "What is Essential Air Service?," Office of Aviation Analysis, U.S. DOT, 1998.

**Table 2: EAS Program – Communities Served,
Appropriations and Funding Sources**

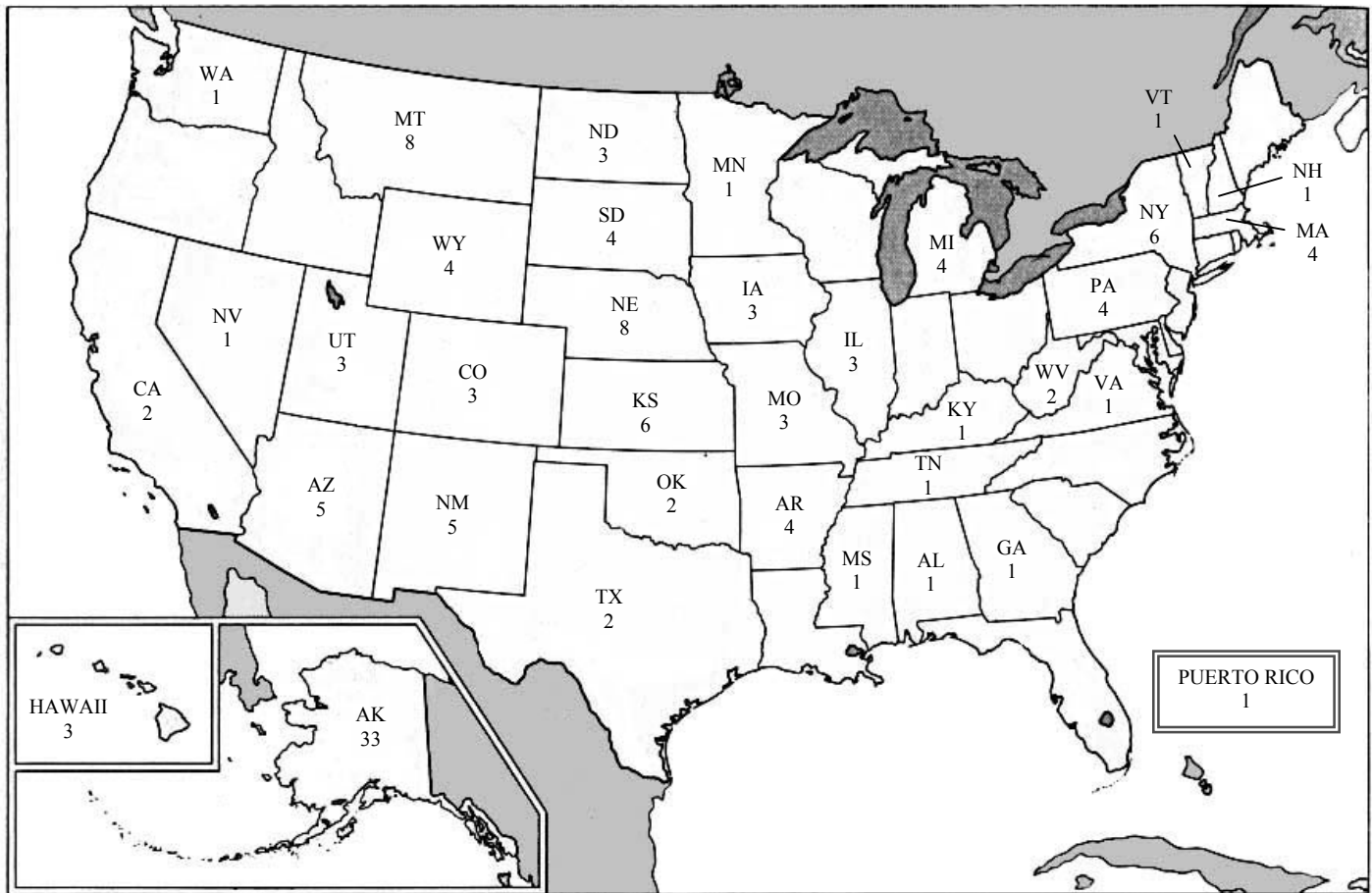
Fiscal Year	Communities Served	Appropriations (US\$millions)	Funding Source
1979	383	68.9	General fund
1980	405	76.1	General fund
1981	352	86.3	General fund
1982	363	65.9	General fund
1983	168	48.4	General fund
1984	146	50.8	General fund
1985	148	52.0	General fund
1986	138	28.0	General fund
1987	135	30.0	General fund
1988	153	28.5	General fund
1989	143	31.6	General fund
1990	119	30.6	General fund
1991	123	26.6	General fund
1992	130	38.6	FAA * Airport and Airway Trust Fund
1993	126	38.6	FAA Airport and Airway Trust Fund
1994	112	33.4	FAA Airport and Airway Trust Fund
1995	106	33.4	FAA Airport and Airway Trust Fund
1996	97	22.6	FAA Airport and Airway Trust Fund
1997	95	25.9	FAA Airport and Airway Trust Fund
1998	101	50.0	FAA Airport and Airway Trust Fund
1999	100	50.0	FAA Airport and Airway Trust Fund
2000	106	50.0	FAA Airport and Airway Trust Fund
2001	115	50.0	FAA Airport and Airway Trust Fund
2002	123	113.0	\$52.1 million from general fund \$50 million from FAA Airport and Airway Trust Fund \$10.9 carryover funds
2003	126	113.0	Unknown

Source: U.S. Department of Transport.

* FAA: Federal Aviation Administration.

Figure 1 shows the distribution of communities with subsidized essential air service, by state and territory. The benefits of the program are geographically broad, covering the majority of the states in the continental United States as well as Alaska, Hawaii and Puerto Rico.

Figure 1: Distribution of Subsidized Communities in Continental United States, Alaska, Hawaii and Puerto Rico



Sources: U.S. Subsidized Essential Air Service Report, 1 June 2003, and Alaskan Subsidized Essential Air Service Report, 1 June 2003.

E. Outlook

The success of the EAS program has been somewhat limited. The government found that, in many cases, subsidizing service did not facilitate the development of services that would be supported by market forces. As well, basic air service to many communities has been eliminated due to funding shortages, in spite of the program's mandate to maintain service. It seems that this program survives due to its popularity in rural America and the relatively strong representation of rural areas in the Senate.

The U.S. General Accounting Office (GAO) released a report in January 2003 on options for enhancing the long-term viability of the EAS program. The GAO reported that the costs of the program have grown exponentially while passenger traffic on subsidized services has

declined. One reason for the decline is travellers' increasing willingness to drive to hub airports to access low-cost carriers' services. The GAO identified four options for enhancing the EAS program's long-term viability. These include: targeting more remote communities; achieving a better match between capacity and community use; consolidating service to multiple communities into regional airports; and changing carrier subsidies into local grants.

The Federal Aviation Act, which enables the EAS program, is due for reauthorization in 2003. The House of Representatives and the Senate prepared different versions of the Act earlier this year and submitted them to a conference committee to produce a final version. The conference committee then submitted its version of the Act to the House of Representatives and the Senate for their votes during the summer. Voting on the reauthorized Act has not yet been completed.

If passed and signed, the reauthorized Federal Aviation Act will reflect some of the GAO's recommendations. The proposed new version of the Act incorporates five or six pilot programs to test alternate ways to administer the program. The pilot programs include initiatives to: provide grants to some communities to manage and pay for their own transportation system; buy out some communities' eligibility for funding so that they can use the money for other transportation projects; and require that some communities pay 10% of the EAS subsidy costs for a three-year period.

SMALL COMMUNITY AIR SERVICE DEVELOPMENT PILOT PROGRAM

A. History

The second federal program to provide assistance in the provision of air service is quite recent. The Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR-21), passed by Congress in 2000, authorized funding for the Small Community Air Service Development (SCASD) Pilot Program. The program was created to improve access to the national air transportation system from airports that suffer from infrequent service or high airfares, through public-private partnerships. The pilot program was scheduled to run for three years, beginning in the 2001 fiscal year.

The SCASD program's mandate is similar to that of the EAS program, but broader; and the SCASD program has less exclusive eligibility criteria.

B. Eligibility

Up to 40 communities per annum can participate in the SCASD program, although no more than four from any one state.⁽⁸⁾ The law requires the DOT to give priority consideration to communities or consortia of communities that meet the following criteria:

- Air fares are higher than the average air fares for all communities.
- The community or consortium will cover, from local sources other than airport revenues, a portion of the cost of the activity to be assisted under the program.
- The community or consortium has established, or will establish, a public-private partnership to facilitate air carrier service to the public.
- Assistance will provide material benefits to a broad segment of the travelling public, including businesses, educational institutions and other enterprises, with limited access to the national air transportation system.

Applicants are not required to share in the costs of the proposed program or project, but priority will be given to those that do. Communities participating in the EAS program are also eligible for SCASD funding, and other small airports without air service may also apply. Communities with airports that are larger than a small hub are not eligible for this program.

Grant proposals have no set format, but the DOT identifies key issues that should be covered in its order soliciting grant proposals. First, the applicant is to describe the current air service situation, including an analysis of needs and deficiencies. As well, the public-private partnership undertaking the project(s) should be defined in terms of administrative and management roles as well as funding contributions. The applicant is to provide some assurance that its own contribution to the funding would be expended in the manner proposed. Finally, the proposal should describe how the success of the program or project would be monitored.

Communities may use their grants to develop creative solutions to their air service problems by making the funds available to:

- 1) an air carrier as a subsidy to provide air service for a period not to exceed three years;
- 2) an airport to create incentives for an air carrier to start service; and

(8) A consortium of communities may also apply and count as one community.

- 3) an airport to implement other appropriate measures to improve air service, both in terms of the cost to consumers and the availability of the service. Such measures may include the marketing and promotion of air service and enhanced utilization of airport facilities.

C. Administration

For the 2003 fiscal year, the DOT received 170 proposals from 46 states requesting more than US\$104 million in assistance. The DOT selected 35 applicants, representing 60 communities, from 34 states and Puerto Rico to receive SCASD grants in that year.

Most grants were for programs that have a number of components – usually a marketing component and some initiative to reduce the risk to air carriers offering new air services. For example, the community or consortium may use the grant to set up a travel bank, purchase tickets in advance or otherwise guarantee air carrier revenue. Among other things, SCASD funding may also be used to cover landing fees, provide free advertising or otherwise reduce the operating costs of new air services.

Specific programs and projects selected to receive grants in 2003 include:⁽⁹⁾

- upgrading existing services to pressurized aircraft;
- pursuing services from a low-cost carrier;
- pursuing services from a second carrier;
- expanding services to more destinations from different airlines;
- subsidizing airfares;
- introducing air services at an airport that did not have any services;
- conducting demand feasibility studies;
- marketing initiatives for EAS program services; and
- extending seasonal services into year-round services.

(9) Order Awarding Grants, U.S. Department of Transportation, Docket OST-2003-15065.

Funds are not awarded in a lump sum at the beginning of the fiscal year; rather, they are used to reimburse the program participants after authorized expenditures are made. While the grants are allocated on an annual basis, the payments continue for as many years as the approved program generates expenses for the applicant.

Currently, no employees are dedicated to administering the SCASD program. As it is still a pilot program, its operations and management are included in the responsibilities of existing DOT staff.

In the 2003 fiscal year, the smallest grant awarded was for US\$20,000 and the largest was for US\$1.5 million. On average, grant applicants requested between US\$400,000 and US\$500,000. More than half of the applicants in 2003 proposed to contribute at least 20% of the total program or project costs.

D. Funding

AIR-21 authorized \$20 million for the program in the 2001 fiscal year and \$27.5 million in each of the following two years. However, Congress did not appropriate any funds for the program in 2001, and only US\$20 million for it in each of 2002 and 2003. Funds were sourced from the FAA Airport Improvement Program Fund.

Table 3: SCASD Pilot Program – Appropriations and Funding Sources

Fiscal Year	Appropriations (US\$millions)	Funding Source
2001	–	–
2002	20	FAA Airport Improvement Program Fund
2003	20	FAA Airport Improvement Program Fund

Source: U.S. Department of Transport.

E. Outlook

The Federal Aviation Act, due for reauthorization in 2003, contains provisions for both the EAS and SCASD programs. Voting on the reauthorized Act has not yet been completed, but the version developed by the conference committee reportedly provides for continuation of the SCASD program. If passed, this will no longer be a pilot program and will have authorization for US\$35 million per year in funding for the 2004–2008 fiscal years.