COMMENTS OF THE
AIR TRANSPORT ASSOCIATION OF AMERICA, INC.
BEFORE THE
PRESIDENT'S ADVISORY PANEL ON TAX REFORM
APRIL 1, 2005

President Bush has established the Advisory Panel on Tax Reform to recommend to him ways to reform Federal tax laws to make them simpler, fairer, and better configured to promote growth in our economy. The Air Transport Association of America, Inc., which represents the larger U.S. passenger and cargo airlines, submits these comments in the spirit of that undertaking.[1]

This is a decisive time for the U.S. airline industry, the customers that it serves, and the communities and businesses that its services benefit. The industry is struggling to recover from the worst financial crisis it has ever experienced. The numbers portray the dismal situation: since 2001, U.S. airlines have eliminated 129,000 jobs and suffered an estimated $33 billion in losses. Analysts project a $5 billion loss for the industry in 2005. Five U.S. airlines are in bankruptcy, with others in perilous financial condition. Yet, Federal excise taxes and user fees continue to stymie the efforts of the nation's airlines to right themselves financially. Self-help alone, therefore, will not produce a successful recovery. The Federal Government must fundamentally realign its aviation tax and fee policies if the U.S. airline industry is to return to financial health.

[1] ATA's members are: ABX Air, Alaska Airlines, Aloha Airlines, America West Airlines, American Airlines, ASTAR Air Cargo, ATA Airlines, Atlas Air, Continental Airlines, Delta Air Lines, Evergreen International Airlines, FedEx, Hawaiian Airlines, JetBlue Airways, Midwest Airlines, Northwest Airlines, Polar Air Cargo, Southwest Airlines, United Airlines, UPS Airlines, and US Airways. ATA's associate members are: Aerovías de México, Air Canada, Air Jamaica, and Mexicana de Aviación.

The Administration has been emphatic about the need to reduce taxes to encourage economic growth. As the President has said, "If you want something to flourish, don't tax it."[2] Treasury Secretary Snow has stated, "Economics tells us that anything you tax, you get less of."[3] Moreover, Alan Greenspan made the same point in his March 3rd remarks before this Panel when he said, "Any tax increase inhibits economic activity in one way or another. Whatever you tax, you get less of."[4]

Unfortunately, the government is not applying this sound advice to the taxation of commercial aviation. The aviation excise taxes-and-fees problem is serious, long standing and worsening. The Federal Government has increasingly assigned airlines the obligation of paying for or collecting taxes and fees to pay for aviation security functions, which are functions that are intrinsically governmental responsibilities because they benefit society as a whole. They should be funded accordingly. The most recent example of this shifting of responsibility to the private sector is the President's Fiscal Year 2006 budget, which proposes to increase the Passenger Security Fee by $3.00, from $2.50 to $5.50 per air travel segment.[5] This would raise the airline industry's annual overall aviation tax-and-fee contribution to more than $17 billion from its present level of $15.8 billion.

---

[2] Remarks by the President in a Conversation on the Benefits of Health Care Information Technology, Department of Veterans Affairs Medical Center, Baltimore, MD, April 27, 2004, available at http://www.whitehouse.gov/news/releases/2004/04/20040427-5.html

[3] Prepared Remarks of Secretary of Treasury John W. Snow, Opening Statement for the President's Economic Forum, Panel on Tax and Regulatory Burdens, December 15, 2004, available at http://www.treas.gov/press/releases/js2151.htm

[4] http://www.progressforamerica.com/1101-341.1101-030405B.html

[5] The increased fee would be capped at $8.00 per one-way trip.

The following table summarizes the excise taxes and fees that the Federal Government imposes, or sanctions, on passenger air transportation.

TAX OR FEE (EFFECTIVE JANUARY 1, 2005)	RATE	UNIT OF TAXATION
Ticket Tax	7.5%	Domestic air fare
Flight Segment Tax	$3.20	Domestic enplanement
Passenger Security Fee	$2.50	Enplanement at U.S. airport
Airport Passenger Facility Charge	Up to $4.50	Enplanement at eligible U.S. airport
International Departure Tax	$14.10	International passenger departure
International Arrival Tax	$14.10	International passenger arrival
Immigration and Customs Enforcement User Fee	$7.00	International passenger arrival
Customs and Border Protection User Fee	$5.00	International passenger arrival
Animal and Plant Health Inspection Service Passenger Fee	$4.95	International passenger arrival

In addition to these passenger-related levies, a 6.25 percent tax is imposed on waybills for domestic air freight shipments. Airlines pay the Federal Government over $300 million annually in Aviation Security Infrastructure Fees. They are also charged an Animal and Plant Health Inspection Service inspection fee of $70 per international flight arrival. Moreover, the Federal Government taxes airlines 4.4 cents per gallon of jet fuel (U.S. airlines in 2004 consumed 13.6 billion gallons of jet fuel in their domestic operations).[6]

The cumulative economic effect on the airline industry of the government's transfer to it of these funding and collection obligations has been enormous. In 1972, taxes and fees amounted to seven percent of the total cost of a single-connection $200 round trip airline ticket in the United States. That proportion has swollen since then. Indeed, the pace of that growth recently accelerated. Increased Passenger Facility Charges, which are Federal Aviation Administration (FAA)-approved airport fees that are

---

[6] Descriptions of the aviation excise taxes and fees listed above, and information about taxes on air carrier sales and operations can be found at http://www.airlines.org/econ/d.aspx?nid=4919.

collected on passengers' tickets, and the introduction of the Passenger Security Fee, which is also collected on passengers' tickets, have hastened that pace. As a result, government taxes and fees now represent 26 percent of a typical single-connection $200 round-trip ticket. Thus, when a customer today buys that $200 ticket, $52 out of the fare goes to local or Federal governmental agencies rather than to the airline. This unrelenting revenue squeeze has been catastrophic for the U.S. airline industry.

The displacement of aviation security funding and collection, and the transformation of what the funding is applied to are illustrated by what has occurred with the FAA's aviation trust fund, known formally as the Airport and Airway Trust Fund. When the FAA was established in 1958, general revenues funded it. In 1970 Congress established the aviation trust fund, which was financed by a tax on airline tickets (known as the "ticket tax") and cargo shipments (known as the "waybill tax"), for the purpose—at the time, the sole purpose—of financing certain categories of aviation-related capital improvements, such as the construction of new runways. However, the original principle of tying the trust fund to capital improvements that would directly benefit airlines and the flying public was abandoned years ago. The adverse consequences of this abandonment are twofold. First, revenues from the ticket tax and the waybill tax now fund non-capital activities, including the operation of the FAA. Second, aviation infrastructure is not receiving the capital funding that it should. This is a profound reorientation of aviation funding that has not served the public interest. Most notably, it has prevented the FAA from increasing the air traffic control system's capacity, which in turn has led to unnecessary delays, increased airline operating costs and unnecessary environmental impacts.

Another example of transforming airlines into tax collectors is the jet fuel tax collection provision in section 853 of the American Jobs Creation Act of 2004, Public Law No. 108-755. That provision was included in the Act because lawmakers concluded that untaxed jet fuel was being diverted for use as highway diesel fuel, without the appropriate excise taxes being paid. However, the remedial provision that Congress enacted places much of the financial and administrative burden of correcting this surface transportation-use problem directly upon air carriers. Effective January 1, 2005, at airports where jet fuel is delivered to the airport by trucks rather than by pipeline (amounting to about 20 percent of total fuel usage), airlines must pay a federal excise tax of 21.9¢ per gallon of fuel. Since the actual excise tax applicable to jet fuel used in commercial aviation is 4.4¢ per gallon for domestic flights, and is zero for international flights, airlines must file for refunds of or credits for the excess tax originally paid. As a result, on an annual basis, airlines are being forced to pay $648 million in taxes upon purchase of this fuel, and then file for refunds or credits amounting to $520 million. This new law thus (1) requires airlines to grossly overpay taxes and thereby severely financially penalizes them; (2) imposes an additional administrative burden on airlines; and (3) places a significant new burden on the Internal Revenue Service to handle airline refund and credit claims. None of these outcomes represents good public policy. Collecting from airlines several times as much tax as is actually due to remedy a surface transportation tax compliance problem illustrates how wayward aviation tax and fee policies have become.

Airlines today pay $11 billion a year into the aviation trust fund; however, neither they nor their customers receive services worth anything approaching that amount.

About $6.5 billion of this sum goes into financing the FAA's operating budget, not its capital budget. Furthermore, a significant portion of airline trust fund contributions is spent on services for general aviation—the operation of private aircraft, including corporate jets—instead of on services for air carriers and their passengers. Security fees impose an additional financial burden on airlines. After 9/11, despite the stated Federal policy that aviation security is national security—and presumably, therefore, is a governmental responsibility—Congress imposed the Aviation Security Infrastructure Fee (ASIF) and the Passenger Security Fee (also known as the September 11th Fee). Airlines' ASIF payments total more than $300 million annually. Passenger Security Fee payments totaled an estimated $1.75 billion in fiscal year 2004. Imposition of these fees confirmed what has become the unmistakable trajectory of the government's aviation funding policy: use airlines as tax payers and tax collectors to fund governmental services that provide society-wide benefits and protections. It also highlights the government's failure to consolidate the six Department of Homeland Security Fees imposed on the airline industry into one lower overall fee.

The problem with these fees and the other taxes and fees summarized on page 3 is that taxing a consumer transaction does not mean that the consumer pays the tax. Airlines absorb Federally-imposed aviation taxes and fees because they do not have pricing power today. Airline customers exhibit intense price sensitivity; in economists' parlance, elasticity of demand. The change in the overall level of spending on air travel reflects this marketplace reality. Spending in the United States on air transportation over the last few decades had remained in a narrow band between 0.9 and 1.0 percent of GDP. Since 2001, however, spending on air travel has fallen to 0.7 percent of GDP. This drop reflects passengers' unwillingness to pay for air transportation at the price levels that they paid only a few years ago. This is a permanent change in consumer behavior. Although airlines can fill up their aircraft with passengers, they cannot charge fares that will enable the industry to come anywhere near breaking even.[7]

The U.S. airline industry has worked hard since 9/11 to right itself financially. Much more needs to be accomplished before the industry returns to financial health. An indispensable element of this industry's recovery will be a fundamentally reformed Federal aviation taxes-and-fees policy. Such impositions have increasingly become dead weight for the U.S. airline industry. Continuing to consign to this critical industry the role of aviation's chief taxpayer and tax collector will rob it of the vitality needed to maximize its contribution to our nation's economy. More specifically, this means that the Federal Government must:

- Unfetter airlines from their role as aviation's chief funding source and tax collector.
- Treat airline and airport security as national security. There is no justification for putting the onus of taxation for national security on just the airlines and their customers.
- Reformulate in a fair, cost-based manner the Airport and Airway Trust Fund when it expires on September 30, 2007. The fund, which was created to maintain and enhance aviation infrastructure, is now being used to provide a majority of the funding for FAA operations, thus inequitably relieving the general revenue fund of that requirement. As a result, the aviation system capacity that we need is not available.

With these changes, the U.S. airline industry will be relieved of overwhelming impediments to its recovery efforts.

---

[7] The 2004 run-up in oil prices provides a clear example of the powerful pricing restraints under which the airline industry operates. Increased fuel costs in 2004 added $6.2 billion to airline industry expenses over 2003 and generated over 60 percent of the industry's estimated total 2004 loss. Unlike other industries, however, the airline industry could not recover that enormous cost increase from its customers. Just as airlines cannot pass on fuel costs to their customers, they cannot pass on taxes and fees to them.