

PRIVATIZING AIRPORTS  
by  
Robert W. Poole, Jr.

I. INTRODUCTION: WHY PRIVATIZE AIRPORTS?

Airline deregulation has set off an unprecedented boom in commercial aviation. U.S. airlines carried 447 million passengers in 1987, nearly double the pre-deregulation level of 240 million a decade before. And traffic is expected to double yet again by the year 2000. Yet this huge increase in activity must be handled by an air traffic control (ATC) and airport system that is little changed from the days before deregulation.

In enacting the Airline Deregulation Act of 1978, Congress freed up the airlines to compete and grow, but left the essential infrastructure--the airports and ATC system--in their static, bureaucratic pre-deregulation condition. The result is a growing set of problems, most notably delays, congestion, and questions about safety levels.

A. The Need for More Capacity

No major new U.S. airport has been built since 1974, when the Dallas/Ft. Worth airport was opened. And only one such new airport is even on the drawing boards today--a replacement for Denver's Stapleton. If present trends continue, a major airport capacity crunch is very likely. Already, the Federal Aviation Administration lists 17 major airports as "seriously congested," and projections indicate that some 50 airports may reach that point by the year 2000. [1]

The problem is not as simple as some would portray it. Many aviation interest groups blame Congress and/or the Administration for consistently failing to spend all the monies which are accumulating in the Aviation Trust Fund (which is fed by several aviation user taxes, primarily the 8% tax on airline tickets). While reprehensible, this underpending is only a symptom of the basic problem.

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How airports are funded is the underlying problem. The present system diverts resources to the wrong place, and poorly uses the capacity we already have. The FAA allocates airport grant funds according to a politically negotiated formula which redistributes large sums from the major airports (where most of the ticket tax collections originate) to hundreds of smaller commercial airports and thousands of general aviation airports. Thus, the system reallocates capital funds from those places where the needs are most pressing to other locations whose needs are nowhere near as great.

If airports operated as businesses, they would price their services the way other businesses do (e.g., the telephone system), with prices varying in accordance with demand. Unfortunately, the present airport system fails to use market pricing to allocate scarce capacity; hence, much of that capacity is wasted. Charging more to land or take off at peak hours would shift some users away from those peaks, to times of day where there is spare capacity. And charging all aircraft based on the value of the service (rather than based on the weight of the aircraft) would shift some non-airline users away from congested hubs to nearby reliever airports, once again making more effective capacity available at the hubs.

In addition, higher prices for peak-hour services would generate additional revenues directly at the point of need, to finance additional capacity. Most hubs have long lists of unmet investment needs by which they could increase their capacity, but they lack the funds to embark on them.

In many ways, today's shortage of airport capacity has stimulated much of the recent thinking about airport privatization. To keep pace with the needs of a dynamic, fast-growing airline industry, we need corresponding changes in the organization, motivation, and operation of our major airports.

## **B. Fostering Competition at Hubs**

A second, growing problem is the phenomenon of concentrated hub airports. Though the airline industry on the whole is highly competitive (with no carrier holding more than 16% of the market), at about a dozen medium and large hubs, only one or two airlines provide a majority of all service. A recent General Accounting Office study found that airline yields are 27% higher at 15 concentrated hubs than at a sample of 38 unconcentrated hubs.[2] A growing percentage of destinations is served by only a single airline from such hubs. In short, the airline industry has developed disturbing pockets of near-monopoly, leaving passengers from those cities with fewer choices and higher prices.

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Two factors enable one or two airlines to attain such dominant positions at hubs. In many cases, the supply of gates is less than the demand, and the dominant carrier has managed to gain control over their allocation--and over the possibility of expansion. In other cases, the runways and landing aids are the limiting factor, restricting capacity below what is demanded. Here, too, existing policies and institutions have led to a few airlines gaining control of most of the slots, with little possibility for either expansion of their number or for true market exchanges.

It is widely--and probably correctly--believed that private-sector owners of airports would bargain more aggressively with airlines about gates and slots than do the present municipal or port authority owners. An airport business enterprise would be far less likely to allow its destiny to be controlled by one or two major tenants. Thus, advocates of more-competitive airport access have begun to consider privatization as a means to that end.

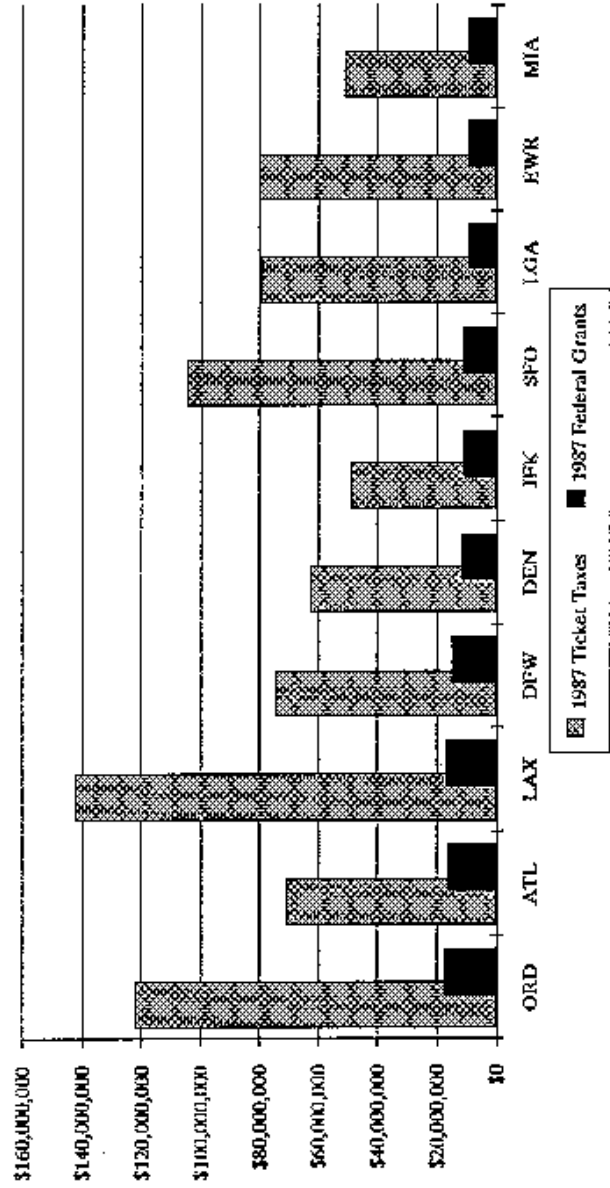
### C. Freeing Up Cities' Capital

From a national perspective, airport privatization is attractive as a way of generating increased investment in airport capacity and addressing the problem of concentrated hubs. City officials are also concerned about hub-monopoly problems which may make their city a less attractive place in which to locate. But municipalities have a far stronger reason to investigate selling their airports.

A medium or large hub represents an investment of hundreds of millions (and in a few cases, more than a billion) of dollars. Yet cities are unable to realize a direct financial return on this investment. Conditions attached to federal airport grants require that revenues derived from airport operations remain on the airport. In other words, the city cannot use its airport as a net revenue generator for the city budget. Moreover, these huge and valuable properties (often totaling several thousand acres) are exempt from property taxation, which is typically the municipal-city's largest single source of revenue.

Thus, at a time when cities have vast unmet needs, ranging from infrastructure repair and expansion to huge unfunded pension liabilities, their airports represent a major source of capital that is locked away, untouchable. Privatization offers cities a way of tapping that capital, while simultaneously improving the airport. Selling the airport yields the city a major one-time windfall, puts the property back on the tax rolls, and sets in motion increased (privately funded) investment which will increase the property's value in years to come.

THE LARGEST AIRPORTS  
 1987 ESTIMATED TICKET TAX GENERATED AND ENTITLED TO FEDERAL GRANTS



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## II. TYPES OF AIRPORT PRIVATIZATION

Privatization is a broad term, which covers a variety of ways in which functions and responsibilities are shifted from the public sector to the private sector. The most common forms of privatization are (1) contracting out of service delivery to a private firm, (2) long term franchising of a firm or consortium to finance, build, and operate a new facility (with ownership eventually reverting to government), and (3) sale of a government enterprise to private owners, to be operated henceforth as a private business. All three types of privatization already exist in the case of airports.

### A. Contract Operation of Existing Airports

The most common form of privatization is the management contract, in which a private firm is hired by the municipality or airport authority to operate the airport, often with considerable authority to make decisions in a businesslike manner. Several American and British firms are actively involved in this business.

The largest U.S. airport operated by a private firm is the Burbank (California) airport. Owned by an airport authority set up by the cities of Burbank, Glendale, and Pasadena, the airport has been operated under contract since 1978 by Lockheed Air Terminal, a division of the giant aerospace firm. Burbank ranks 59th in size (as measured by annual passenger enplanements) among commercial airports.

Altogether, Lockheed operates at 22 airports or terminals in the United States and overseas. Among the other larger airports are Rickenbacker Airport in Columbus (Ohio)—a former Air Force base and a major hub for Flying Tiger (now Federal Express), Republic Airport on Long Island—which is served by commuter airlines, and Stewart International Airport—a former Air Force base north of New York City (where American Airlines will begin scheduled service in 1990).

Another important contract operator is Pan Am World Services (recently acquired by Johnson Controls, Inc.). Since 1977, Pan Am has operated the White Plains airport in New York's Westchester County, an important reliever airport for the metro area. It also runs Atlantic City International, Bader Field, and Teterboro Airport, all in New Jersey. Another contract operator is Avco International Services (now a division of Combustion Engineering), which operates the airports at Morristown (New Jersey) and Grand Canyon (Arizona).

British firms are also in the contract-operation business. International Aeradio Ltd. (IAL), a subsidiary of British Telecom, provides both airport-management and air traffic control operations under contract to governments in several dozen countries, with operations in the U.K., Africa, and the Middle East. In addition, British Airports Authority (owner of seven airports in England and Scotland) operates four other British airports and has set up a U.S. division called Air Terminals, Inc. to seek airport-management contracts in the United States.

What contract management brings to municipal airports is a far more businesslike method of operation. Many municipal airports—especially those smaller than the top 100—are money-losers for their communities. Morristown, Teterboro, and White Plains airports were all losing money when their operation was contracted out—and all were put solidly into the black within a year or two under contract operation. Private management means both cost-saving efficiencies and increased revenues.

Short-term changes, such as a computerized landing-fee-billing system and more efficient use of staff, make quick improvements in efficiency. In addition, firms which operate a number

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of airports can take advantage of economies of scale via centralized management of various airport functions and buying fuel, equipment, and services in bulk.

But the longer-term benefits of contract operation result from aggressive management of the airport's assets. The private operators invest their own funds in capital improvements, and they attract significant new private investment in airport-compatible facilities: hangars, warehouse space, office buildings, hotels, etc. This leads to substantial increases in airport revenue over time.

### **B. Build-Operate-Transfer for New Airport Facilities**

In civil engineering and heavy construction, the term Build-Operate-Transfer (B-O-T) refers to the practice of obtaining large-scale infrastructure projects via long-term contract or franchise with a private consortium. In exchange for the franchise, the consortium will design, finance, build, and operate the facility, deriving revenues from user charges to recover its investment over the life of the contract (typically from 20 to 40 years). At the end of this period, ownership of the facility reverts to the government.

B-O-T arrangements have been used for more than 30 years to build major motorways and tunnels in Europe, especially in Italy and France (and most recently, with the Channel Tunnel). Toll roads, bridges, and tunnels have been or are being built via B-O-T in Australia, China, Hong Kong, Indonesia, Malaysia, South Africa, and Turkey, among other countries. B-O-T is also increasingly used in Third World countries to provide new power plant facilities. In the United States, the principal use of B-O-T has been for new wastewater treatment plants and waste-to-energy plants during the past decade. But the concept is now being applied to toll highways in California and Virginia.

B-O-T arrangements for airports are one of the newest applications of this idea. In 1987 in Canada, the team of Huang & Danczkay and Lockheed were selected to finance, design, build, and operate a new \$300 million, 24-gate terminal at Toronto's Lester B. Pearson International Airport. In 1988 a team consisting of Fluor, Lockheed, and Lewis Enterprises, plus three Turkish firms, was selected to develop a \$200 million, 18-gate terminal at Ataturk International Airport in Istanbul. Upon completion of the terminal in 1992, Lockheed will take over operating the entire airport under contract. And in 1989 work began on a new terminal at Birmingham (England) International Airport, being financed and developed by Euro-11nb, a public-private consortium including the airport (with 25%), several British firms, and Lockheed. Both the new Hong Kong airport on Lantau island and the new Macao airport will be financed, built, and operated by public-private consortia with majority private ownership.

Airport B-O-T projects of this type offer several advantages over conventional airport development. One is the speed with which the project can be carried out, in the absence of typical public-sector red tape and bureaucracy. Both the Toronto and the Istanbul projects are being built using fast-track design-build schedules. The Toronto project will take 3 1/2 years, compared with Transport Canada's estimate of 7 years if it had done the terminal in the conventional manner. In addition, no public funds are required for such projects; the existence of the contract or franchise (assuming sound financial projections) is sufficient to obtain debt and equity capital from the financial markets.

### **C. Sale of Existing Airports**

Selling existing commercial airports, to be operated thereafter as privately owned businesses, is the newest form of airport privatization. While there were proposals in the early Reagan years that the federal government sell its two commercial airports (Dulles International and

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Washington National), the Administration yielded to local political pressures to divest those airports to a newly created state government authority, on a long-term lease basis.

The first actual airport privatization via sale was the British government's sale of British Airports Authority. BAA had been created as an independent government authority in 1966, with ownership of London's Heathrow, Gatwick, and Stansted airports and Scotland's Aberdeen, Edinburgh, Glasgow and Prestwick airports. In 1983, BAA was designated for privatization via a public share offering; enabling legislation was enacted by Parliament in 1986. In July 1987, 500 million shares were sold to the public, generating approximately \$2 billion for the Treasury.

Today BAA operates all seven airports, subject to regulatory review of its aeronautical charges. It operates essentially as a monopoly public utility, though without the burdensome form of rate regulation typical of U.S. public utilities. According to a 1989 study [3], privatization of BAA offers several advantages. These include greater access to financing for capital improvements, more productive use of land and other assets, and diversification into other lines of business. This includes ground transportation, hotels, retailing, property development, and management of other airports under contract.

A number of other governments overseas are pursuing airport privatization. The Danish government in 1989 announced plans to sell the Copenhagen international airport, Kastrup. The sale is expected to be a public offering, similar to that of BAA. New Zealand has corporatized its major airports, and in November 1989 announced that it would sell the government shares in the three major airports (Auckland, Christchurch, and Wellington) in 1990. Malaysia has carried out a feasibility study of converting its six major airports to private operation. Even Poland has begun discussing airport privatization with foreign investors.

The Canadian government's Transport Canada, after embarking on an airport defederalization program in 1988, has recently proposed selling some of its 138 airports, including the largest, Toronto's Lester B. Pearson International. Responding to that announcement, BAA has created a joint venture company, Canadian Airports Ltd., 51% owned by a Canadian partner, to seek airport acquisitions.

In the United States, no commercial airport has yet been sold to private enterprise (although Syracuse, NY in 1988 sold its airport cargo facilities). The most serious privatization effort thus far has been that of Albany County, New York, to sell or lease its airport. The county executive announced the pending sale of the airport in 1988, which resulted in offers from the local mass-transit authority and a private consortium (composed of a local firm, British American, Ltd. and Lockheed Air Terminal). The latter offered either a long-term lease or an outright purchase. In December 1989 the Federal Aviation Administration ruled that neither the lease nor the sale was consistent with its interpretation of federal regulations. The county then decided to pursue a management contract with Lockheed, instead.

A detailed near-privatization proposal has been put forward by the Peoria Airport Authority, under which all land-side (non runway/taxiway/ramp) property would be leased to a private firm for 99 years. The plan attempts to gain the benefits of de facto private ownership and operation while keeping the airport eligible for federal grant funds by retaining public ownership of the federally aided air-side property. With the proceeds from the lease (plus federal grant funds), the airport would be able to acquire additional lands for runway and taxiway expansion, in accordance with its long-term growth plan. Additional land adjacent to the new runway areas would be leased to the private airport firm.

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Two other major cities have begun considering selling their airports. Atlanta was approached in 1988 by Merrill Lynch Capital Markets, on behalf of unnamed (but reportedly Japanese) clients about selling the giant Hartsfield International Airport. The model for the deal was reported to be the BAA privatization, and as did the British government, the Atlanta city government would have retained a minority share of the ownership. A figure of \$1.5 billion was cited in several news articles.

In 1989 the Los Angeles Department of Airports commissioned its consultant, John F. Brown Company of Cincinnati, to look into--among other things--privatization of Los Angeles International and possibly the department's other three airports. California Assemblyman Richard Katz, head of the Assembly Transportation Committee, has called for serious investigation of airport privatization in California, as a way of enabling cities to gain direct financial benefits from their airports.

### III. TURNING AIRPORTS INTO BUSINESSES

#### A. The Current Funding Problem

The top 50 airports (large and medium hubs) account for 81 percent of all airline enplanements in this country. It is these airports whose capacity is especially strained by the projected growth of airline traffic over the next two decades. Hence, it is these airports which most crucially need to operate like businesses, with appropriate incentives and ability to meet the growing demand for their services.

The present system of airport finance, largely influenced by the airlines, is poorly suited to this task. In a market economy, shortages trigger price increases; those higher prices tend to increase profits, thereby attracting investment to the area in question. That, in turn, leads to added capacity, which relieves the shortage.

This kind of feedback system does not operate in the airport business, because airports are operated on a non-commercial basis. The primary customers--aircraft and passengers--are not charged direct market prices for the airport's services. In fact, the general model is for the airport operator to derive the bulk of its operating revenue from tenants and concessionaires--airline gate lease payments, shop and restaurant lease payments and/or percentages of their turnover, rental car company fees, etc.--with any residual need for revenue made up from landing charges. Typical landing fees are based on the weight of the aircraft, not on the value of the service. Passengers typically pay no direct charge for using the airport.

The majority of major airport capital expenditures are derived from the sale of tax-exempt revenue bonds, backed by long term lease payments from airline tenants. Only a minority of capital funding--just 20 percent for large hubs and 25 percent for medium hubs--comes from federal grants under the Airport Improvement Program. These funds derive principally from the 8 percent federal tax on airline tickets which feeds the Aviation Trust Fund.

Yet perversely, this system of federal grant funds serves primarily to channel resources from the airports with the most serious capacity problems to those with much less need for capital spending. Table 1 estimates the amount of funds generated by the ticket tax at each of the top 50 airports and contrasts this sum with the amount returned to the airport in the form of airport "entitlement" grants.<sup>[4]</sup> Los Angeles International, for example, generates \$142 million in ticket taxes but gets back only \$16.6 million. On average, these major airports get back only 18.5% of the ticket tax funds generated by passengers originating there. At a time of growing



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capacity problems, the present mechanism systematically undercuts the potential market mechanism whereby shortages would lead to increased revenues to fund expansion.

### **B. The Potential Increased Capacity of Existing Airports**

Privatization would provide the means for major capital investments in the nation's airports. Capital is needed for additions to the runway system and for upgrading the technology used in landing systems. In addition, a pricing system would provide incentives for making greater use of existing capacity that is now wasted. The primary beneficiary would be the travelling public, thanks to fewer delays and less congestion.

Adding main runways is not possible at some major hubs because of the lack of available land (e.g. LaGuardia, Washington National, and Los Angeles International), but space exists to do so at such airports as Kansas City International, Nashville, and San Jose--if sufficient capital were made available.

Another way to increase capacity is to provide separate runways for commuter and business aircraft. These planes are typically slower and much smaller than jet airliners, making for significant improvements in throughput if they can be separated from airliner traffic patterns. At Atlanta's Hartsfield, for example, commuter planes account for 22% of flight operations, but handle only 4% of the passengers.[5] Adding a separate 6,000 ft. commuter runway could increase Hartsfield's jetliner capacity by up to 22%. Similar additions could be made at Boston's Logan Airport, Detroit Metro, and St. Louis Lambert.

At some major hubs, bad weather produces major cutbacks in landing capacity, because only one of the main runways is equipped with an instrument landing system (ILS). Adding ILSs to other runways would make a major difference at Boston, Denver, LaGuardia, and San Francisco. Few airports currently are equipped with the equipment which makes possible fully-automated landings in fog and other poor-visibility weather. Additional capital would facilitate the upgrading of ILSs to this Category 3B capability.

One of the major problems at the nation's busiest hub, Chicago O'Hare, is obsolete air traffic control equipment and insufficient controllers.[6, 7] If O'Hare had the resources and were responsible for its own ATC functions, rather than being dependent on the FAA, modernizing the radars and computers and hiring sufficient tower personnel would have been accomplished years ago. Only in 1989 did the FAA finally adopt a program to offer 20% higher pay to controllers willing to move to Chicago (and several other urban areas with high costs of living and shortages of controllers).

Another way to increase capacity is to permit simultaneous operations on closely-spaced parallel runways. Current FAA regulations permit such operations only if the runways are at least 4,300 feet apart, due to the inadequacy of current radar systems. The new high-tech QuickScan radar, currently being tested at Raleigh-Durham airport, updates the controller's display 10 times more frequently than current radars, making it possible to monitor approaches that are more closely spaced. The FAA estimates that QuickScan will produce a 30% increase in effective capacity at a dozen airports, including Raleigh-Durham, Baltimore, Memphis International, Minneapolis-St. Paul, Dallas's Love Field, and Salt Lake City International.[8] At some airports with limited expansion room, the QuickScan radar may make it possible to squeeze in a third runway where only two are now feasible.

Yet another possible technological fix is microwave landing system (MLS), a successor to the ILS. Among other things, the MLS will permit aircraft to fly curved and segmented approaches rather than only straight-in approaches, as well as using closely spaced

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runways.[9] MLS is currently embroiled in controversy within the airline industry over its cost-effectiveness; its major cost will be up to \$5 billion to equip all airline aircraft.

Increased funding would make possible the kinds of capacity increases discussed above. But market pricing of landings and takeoffs would also lead to net increases in capacity. Even at busy hub airports, congestion (demand exceeding supply) only occurs at certain limited times during each 24-hour period. The rest of the time, there is ample capacity going unused. Charging higher fees for operations during peak hours would shift some of those operations into off-peak time periods (and would also shift some general-aviation activity to nearby reliever airports). It would also generate additional revenues which would help to fund capacity increases.

In a recent study for the Brookings Institution, Steven A. Morrison and Clifford Winston modeled the effects of shifting from today's weight-based landing fees to a system of "marginal-cost" landing fees which reflect the value of airport access at various times of day. They found that a policy of charging such fees and using the revenues to expand airport capacity would lead to net economic gains (reduced airline operating costs, passenger time savings) of \$11 billion per year.[10]

Market-based pricing, in Morrison and Winston's model, would lead to changes in usage at major commercial airports. Many general aviation aircraft would shift to reliever airports or to off-peak hours to avoid higher landing fees. Commuter airlines would shift to a smaller number of larger planes (and might have their landing charges subsidized by the major airlines whose flights the commuters feed). And the major airlines would shift marginal flights away from the (highest-cost) peak hours. All these changes would make greater total use of whatever level of capacity exists at an airport in a given year. And the increased revenues from the new landing fees would pay for major additions to the airport's capacity over a period of years.

### C. Giving Airports Control of their Resources

If major hub airports were fully converted into business enterprises, what resources should they be able to control? Since a major purpose of privatization is to increase capacity, each airport should gain control of those resources which determine capacity. That means (1) physical resources, (2) financial resources, and (3) landing slots.

The physical determinants of airport capacity are the runways and taxiways, the landing aids (ILS, radar, etc.), the control tower and its personnel and computers, and the terminal gates. At present, the airport operator has effective control of the runways and taxiways (though it is constrained by conditions attached to federal grants for those facilities). The landing aids and control tower, however, are owned and controlled by the FAA. And the number and extent of terminal gates and facilities is constrained to a considerable degree at most major hubs by provisions of the lease agreements between the airline tenants and the airport.

A full-fledged privatization policy would transfer title to the landing aids and control tower to the airport operator. This would make the airport the employer of the controllers and other local ATC personnel (maintenance technicians, etc.). Like airline pilots and mechanics, these personnel would still be required to hold FAA licenses and all airport operations would be subject to ongoing FAA safety regulation and oversight, just as are airline flight operations and maintenance. Salaries and working conditions, however, would be determined by the airport company, based on local needs. Hence, the airport would no longer be limited by being unable to attract sufficient controllers. Likewise, the purchase of state of the art computers and radars, and the addition of ILSs to runways not so equipped, would be decisions made locally, rather than in Washington.

TABLE 1  
TICKET TAXES vs FEDERAL GRANTS  
AT LARGE AIRPORTS

RANK BY SIZE	SYMBOL	NAME	1987 ENPLANEMENTS	ESTIMATED 1987 TICKET TAX GENERATED	1987 ENTITLEMENT GRANTS	PERCENT RETURNED
1	ORD	Chicago	27,618,295	\$121,962,400	\$77,689,662	14.5
2	ATL	Atlanta	24,001,009	\$70,764,800	\$16,000,300	22.6
3	LAX	Los Angeles	21,801,305	\$142,400,000	\$16,642,705	11.7
4	DFW	Dallas/Ft. Worth	20,974,098	\$74,756,000	\$14,990,300	20.1
5	DEN	Denver	16,144,504	\$62,503,200	\$11,858,928	19.0
6	JFK	NY-Kennedy	14,652,734	\$49,327,200	\$11,082,689	22.5
7	SFO	San Francisco	14,566,099	\$104,548,800	\$10,830,464	10.4
8	LGA	NY-LaGuardia	12,049,294	\$79,552,800	\$9,113,559	11.5
9	EWR	Newark	11,798,779	\$80,484,000	\$8,924,130	11.1
10	MIA	Miami	11,784,797	\$50,921,600	\$9,025,118	17.7
11	BOS	Boston	11,589,273	\$79,986,400	\$8,898,027	11.1
12	STL	St. Louis	10,152,163	\$37,668,000	\$7,963,906	21.1
13	DTW	Detroit Metro	9,948,572	\$50,207,200	\$7,831,572	15.6
14	HNL	Honolulu	9,735,544	\$43,664,000	\$11,664,279	26.7
15	MSP	Minneapolis/St. Paul	8,966,394	\$44,988,000	\$7,193,156	16.3
16	PHX	Phoenix	8,911,660	\$41,959,200	\$7,157,579	17.1
17	PIT	Pittsburgh	8,723,284	\$27,224,000	\$7,035,135	25.8
18	LAS	Las Vegas	7,802,162	\$35,912,800	\$6,436,435	17.9
19	PHL	Philadelphia	7,692,304	\$50,763,200	\$6,364,998	12.5
20	DCA	Washington National	7,561,677	\$61,690,400	\$6,533,738	10.6
21	MCO	Orlando	7,506,215	\$46,271,200	\$6,244,040	13.5
22	IAH	Houston Int.	7,399,570	\$32,552,000	\$6,951,950	21.4
23	SEA	Seattle	7,178,491	\$52,690,400	\$6,031,319	11.4
24	CLT	Charlotte	6,472,651	\$15,576,800	\$5,572,223	35.8
25	MEM	Memphis	5,341,763	\$15,784,800	\$4,837,146	30.6
26	JAD	Washington Dulles	5,194,902	\$18,766,400	\$4,488,067	23.9
27	SAN	San Diego	5,059,380	\$37,893,600	\$4,653,597	12.3
28	TPA	Tampa	5,002,812	\$35,950,400	\$4,616,828	12.8
29	SLC	Salt Lake City	4,895,326	\$21,524,000	\$4,546,962	21.1
30	KCI	Kansas City	4,698,252	\$22,897,600	\$4,418,864	19.3
31	BWI	Baltimore	4,635,322	\$23,465,600	\$4,377,959	18.7
32	FLL	Ft. Lauderdale	4,338,602	\$31,562,400	\$4,165,591	13.2
33	HOU	Houston/Reobby	3,935,757	\$20,806,000	\$3,506,013	16.9
34	SJU	San Juan	3,642,766	\$20,668,800	\$6,061,977	29.3
35	CVG	Cincinnati	3,642,684	\$19,555,200	\$3,732,745	19.1
36	MSY	New Orleans	3,484,797	\$23,987,200	\$3,630,118	15.1
37	CLE	Cleveland	3,320,978	\$26,736,800	\$3,823,636	14.3
38	BNA	Nashville	3,178,395	\$15,796,800	\$3,431,087	21.7
39	PSX	Portland	2,870,789	\$23,303,200	\$3,230,624	13.9
40	SJC	San Jose	2,863,698	\$19,750,400	\$3,213,404	16.3
41	MWY	Chicago Midway	2,637,704	\$16,229,600	\$1,689,898	10.4
42	SAT	San Antonio	2,514,604	\$16,326,400	\$2,999,493	18.4
43	DAL	Dallas/Love	2,443,995	\$6,948,800	\$2,953,397	42.5
44	RDU	Raleigh/Durham	2,428,389	\$14,083,200	\$2,943,453	20.9
45	IND	Indianapolis	2,426,168	\$17,869,600	\$2,942,009	16.5
46	BOL	Hartford	2,397,226	\$22,794,400	\$3,223,197	14.1
47	DAY	Dayton	2,381,316	\$10,570,400	\$2,913,180	27.6
48	PBI	West Palm Beach	2,320,353	\$19,954,400	\$2,873,229	14.4
49	DBE	Hawaii	2,276,400	\$8,108,800	\$2,728,109	33.5
50	DHT	Ontario	2,271,842	\$17,001,600	\$1,734,840	10.2

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Obviously, an airport company must have the financial resources to take advantage of its new ability to own and control its physical resources. Hence, the second element of privatization would be the freedom to charge market prices for airport services. Specifically, the privatized airport should be allowed to charge (1) market-based landing fees, and (2) passenger facility charges.

At present the legal status of charging fees other than the traditional weight-based landing fees is not clear. The New York Port Authority has charged general aviation aircraft a \$100 peak-hour surcharge at JFK, LaGuardia and Newark since 1986. In 1988, the Port Authority increased the minimum peak-hour charge for commuter (regional) airlines to \$50 (from \$20). By contrast, when the Massachusetts Port Authority (Massport) in 1988 implemented a fee system at Boston's Logan Airport based on a minimum charge of \$100 plus a per-pound charge (which significantly increased the amount paid by general aviation aircraft while decreasing the fees for commercial jetliners), the agency was taken to court by both the Aircraft Owners & Pilots Association and the National Business Aircraft Association. Despite a federal court ruling upholding the legality of the fees, the Department of Transportation ruled that they were "unjustly discriminatory" and could not be charged if Massport were to continue receiving federal funding.

A true market pricing system--unlike Massport's system--would vary the charge by time of day, based on the demand for landings and takeoffs. Hence, it would offer ample opportunity for general aviation users to pay lower prices for use during off-peak hours. In addition, it would be non-discriminatory in that any aircraft wishing to pay the market price to land at peak hours would have the right to do so (unlike Massport's proposed peak-hour system with different rules for eight different types of aircraft, which openly discriminated against smaller planes). Indeed, DOT Associate General Counsel Jeffrey Jacobs has said that DOT would have been receptive to a Massport fee system that included peak-period charges "if it had been done in a reasonable manner."<sup>[11]</sup>

Since 1972, airports have been forbidden to charge passengers directly by an anti-head-tax law. (Prior to enactment of this measure by Congress, some 60 U.S. airports levied some form of per-passenger charge.) The Airport Operators Council International has proposed that this measure be repealed and that the right to charge a per capita fee be restored to airports. Airlines would add this charge on their tickets, and remit the amounts collected each month to the airports imposing the charge. The revenues would be restricted to financing safety and capacity improvements. A \$3 per passenger charge, had it been in place in 1987, would have generated, for example, some \$83 million for O'Hare, \$72 million for Atlanta, \$65 million for Los Angeles International, and \$63 million for Dallas-Ft. Worth. More important, that assured stream of revenues would make it possible to raise 8.33 times those amounts in bonds for capacity expansion.<sup>[12]</sup>

To increase airline competition at airports, it is especially important to give the airports new revenue sources which can be used to float bond issues. Airport expansion today is all too often held hostage to the "majority in interest" clauses of airline lease agreements. Those agreements--in effect at 55 airports, including 15 of the 27 largest airports, according to a recent GAO study <sup>[13]</sup>--give existing airline tenants a veto power over additional bond-funded expansion which would be paid for with lease revenues. Therefore, new airport revenue sources are an essential tool for countering trends toward "fortress hub" monopolization by one or two incumbent airlines.

The final "resource" affecting capacity is the landing slot. In a legal sense, such slots exist only at the four airports designated by the FAA in 1969 as capacity-constrained: O'Hare, JFK, LaGuardia, and Washington National. Slots (the maximum number of operations permitted

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per hour) were once allocated by airline scheduling committees, but since 1986, airlines have been free to sell, lease, or trade such slots. Unfortunately, new-entrant carriers have had difficulty purchasing sufficient slots from established incumbents. The number of slot sales between unrelated carriers has dropped from 110 per quarter in 1986 to 12 per quarter in 1988, according to the GAO.[14] Major carriers do lease slots, but generally not to competitors. And FAA rules allow slots to go unused up to 35 percent of the time during any two-month period. Moreover, when the FAA parceled out slots at the four constrained airports, it gave away assets of considerable market value (as determined by subsequent transactions): \$400,000 at Washington National, \$300,000 at O'Hare, \$200,000 at LaGuardia, and \$100,000 at JFK.

This system is both inefficient and unfair. It is inefficient because carriers which value slots more than their current owners may not be able to get them. And it is unfair both because it is anticompetitive and because the creators of the slots--the airports--are not allowed to benefit financially from the property which they have created. If O'Hare invests resources in creating a new commuter runway which adds 30 slots per hour, it has created those slots--and it ought to be their legal owner. The same is true for the existing slots, all of which result from the investments in capacity made by the airport.

Hence, as part of privatization, airports should be given legal ownership of their landing slots. Existing slots in the possession of airlines should be returned to the airport operator, to be leased out on terms negotiated between the airport and all would-be users, at market prices. For those slots given to an airline by the FAA, no compensation would be due to the airline. But in the case of slots which an airline had purchased, compensation should be paid by the federal government, using monies from the Aviation Trust Fund.

#### **D. General Aviation Access**

The term "general aviation" (GA) refers to all civilian aircraft activity other than that of airlines (including commuter/regional carriers). GA thus includes air taxi service, business & corporate aviation, private flying, and helicopters. A recent study by Willbur Smith Associates estimated the economic impact of both commercial and general aviation; while the former accounts for 92.7% of total aviation economic activity, general aviation's 7.3% amounts to an impressive \$38.1 billion per year.[15]

Of the 271,183 U.S. aircraft making up the general aviation fleet, 87,823 are engaged in some form of business activity. This includes 3,901 jet aircraft, 4,746 turboprop planes, and 73,077 piston-powered planes. Most general aviation activity takes place either at the 16,418 general aviation airports or at the smaller of the 531 commercial service airports (non-hubs and small hubs). Those operations would not be affected by the privatization of large and medium hubs.

But a move toward market pricing at large and medium hubs would have a strong impact on the general aviation operations that do take place at those airports. Some GA operations would move to reliever airports elsewhere in the metro area. Others would shift from peak hours to off-peak times (e.g. 30% of GA traffic shifted out of peak hours at the three New York airports following introduction of the \$100 peak-period surcharge in 1986).[16] In terms of making the best use of scarce landing capacity, such shifts are highly desirable.

General aviation groups (AOPA and NBAA) protest that such shifts would unfairly deprive their members of needed access to major airports. They argue that any shift to market pricing should set aside a certain percentage of operations for GA users, possibly at lower prices than those charged to airlines (much as present FAA policy allocates a fraction of the slots at LaGuardia and Washington National for GA users).

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These arguments should be examined in terms of fairness and equity. The public will understandably have trouble seeing why corporate jets and turboprops should be exempted from having to pay the same \$500 to \$1,000 that a 727 would pay to land. They will also find it hard to understand the need for a nonbusiness Cessna 172 private pilot to be guaranteed a below-market price to land at Los Angeles International when there are a half dozen GA airports within 20 miles.

On the other hand, there may well be a politically compelling case to be made for special treatment for the small-business piston plane which provides air-travel access to a major city from the business's small-town location--at least in those metro areas where reliever airports are distant from business locations. Aircraft owners qualifying for this exemption might be offered subsidies to enable them to pay the market price (somewhat like the subsidies offered to small airlines under the Essential Air Services program). Whether such cases can be defined sufficiently precisely to exclude all but those intended to be covered remains to be seen. But it does seem clear that a company large enough to afford a corporate jet or turboprop should pay the market price, and also that non-business (pleasure) flyers should do so as well, if they wish to take up the scarce and valuable space at large and medium hubs.

Though they are not considered part of general aviation, commuter and regional airline aircraft are also a controversial issue when market pricing is discussed. In the case of Boston's Logan Airport, the Regional Airline Association (representing 77 small carriers) charged that the 1988 Massport fee changes would cut the number of passengers on small airlines using Logan by 8 percent. But during the less than six-month period the new fees were in effect, while the number of commuter flights decreased by 3.1%, commuter passengers actually increased 0.6%, as the airlines increased the size of plane they used at Logan while decreasing the frequency of flights[17]--just what one would expect from market pricing.

No special exemption from market pricing should be granted to commuter and regional carriers. To the extent that such pricing might seriously affect the marketability of their service, it would be in the interest of the major airlines (whose flights they feed) to offer joint fares which would, in effect, subsidize the fares charged on the feeder service.

#### **IV. PRIVATIZATION OF MAJOR HUBS**

If major airports were privatized, as discussed in the previous section, they would be able to operate as businesses. They would raise their own revenues, directly from their customers, and would have control over their own resources (under the regulatory supervision of the FAA for all safety matters, as are the airlines). How feasible would it be to actually privatize the nation's 50 largest commercial airports? What would be the benefits to these airports' present municipal owners? And how would such privatization benefit the national air transportation system? This section addresses these questions.

##### **A. Private Airports Thus Far**

To date, the world has limited experience with for-profit air-carrier airports. The only one in the United States was the Burbank Airport, created by the old United Aircraft Corp. in 1929. Lockheed acquired the airport in 1940, expanding it greatly during the war years, when it was the only commercial airport serving the Los Angeles area. But after World War II when the city of Los Angeles opened LAX, traffic at Burbank declined greatly (dropping from a 1946 peak of 1.2 million passengers to just 271,000 several years later).

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LAX subsequently received many millions of dollars in federal airport grants, for which Burbank, as a privately owned airport, was not then eligible. Although the airport remained profitable, Lockheed, in the mid-1970s, was not. Selling the airport therefore looked attractive both to Lockheed and to the nearby cities of Burbank, Glendale, and Pasadena. The cities created an airport authority which received \$35 million in federal grants to buy the airport, with Lockheed hired to manage it. Subsequently, the authority received another \$12 million in FAA capital grant funds, which were used to rebuild runways, ramps, and taxiways.

Today, however, it is the public sector that is strapped for funds and the private sector that views airports as a growth industry sorely needing capital investment. That explains the enthusiastic investor response to the British government's sale of British Airports Authority in 1987. Following the successful privatization of BAA, national and local governments in other countries have begun to look seriously at selling their airports, as noted in Section II. It is time to take a careful look at the benefits which selling airports would yield.

### **B. Benefits to Local Government**

Why would a city or county wish to sell its airport? One important reason is to increase the availability of capital for airport expansion. Commercial air service is an increasingly important factor in the economic vitality of cities and regions. But airport capacity is failing to keep pace with the growth of air travel. In a recent survey of 183 airports, GAO found that 54 said they had no plans to build any additional gates in the next five years, while another 63 planned to add no more than five gates. GAO analyst Kenneth Mead told a congressional hearing in September 1989, "The airports in our survey cited funding as a major constraint on their ability to expand."<sup>18</sup>

A major factor in Albany County's proposed airport privatization was the private consortium's proposal to expand and modernize the antiquated airport terminal (\$106 million for the first phase). As noted above in section III B, most major airports in the United States have large backlogs of capital projects which they have been unable to fund. Private capital would make a substantial difference in meeting this need.

A second reason for municipalities to privatize is to prevent local air travelers from being taken advantage of by reduced competition at hub airports. The General Accounting Office has found that airline yields (revenue per passenger mile) are 27% higher at 15 concentrated hubs (such as Atlanta, Minneapolis/St. Paul, and St. Louis) than at a sample of 38 unconcentrated hub airports.<sup>19</sup> This means that air travelers who live in those cities and must originate their journeys there are being taken advantage of by the small number of airlines operating from those hubs. Between 1985 and 1988, according to GAO, the number of destinations served by four or more airlines from concentrated hubs decreased by 52%, while the number of places served by only one airline from concentrated hubs rose 25%. Captive consumers in these locations are getting less choice of service at higher prices, compared with airports where competition is prevalent.

It would not be in the interest of a private airport company to link its fate with one or two dominant airline tenants, able to call the shots in determining the airport's future. Instead, a profit-oriented airport operator would seek to remain in control of its destiny. That would mean avoiding such practices as signing long-term leases with majority-in-interest (MII) clauses. Rather, the airport company would seek to gain and retain control of the gates and other resources (as Miami International and Phoenix Sky Harbor airports have done).

In turn, the countervailing power of airline tenants would keep airport charges in check. The airport firm has much to gain by working cooperatively with the airlines. Privately owned

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commercial airports would seek to expand their gate and runway capacity to meet projected demand, actively seeking new airline customers. Such policies would directly serve the interests of air travelers living in the airport's metropolitan area.

Third, from a financial standpoint, a municipal airport is an underutilized asset. Because of federal restrictions in the airport grants program, local governments may not divert airport revenues to their general funds. Hence, airports tend to be operated as, at best, break-even operations. But when the airport loses money, the municipality must stand ready to bail it out. Yet, unlike roads and highways, airports serve only a portion of the community; it is not clear why they should be subsidized by all taxpayers. Moreover, as municipal properties, airports do not pay property taxes, despite occupying vast amounts of very valuable acreage. Municipalities may understandably resist the expansion of airport boundaries to the extent that this would remove even more valuable land from the local tax rolls.

Cities would benefit financially from selling their airports in three principal ways.

One-time asset sale revenue. Major commercial airports are "going concerns," worth hundreds of millions--and in some cases more than a billion--dollars. Table 2 shows that the estimated market value of the largest 50 commercial airports is \$23.5 billion. The estimates for each airport are based on a multiple of its annual enplanements (using 1987 data). There are several possible ways to establish the value of a business, based on its annual revenues, asset values, and other factors. In addition, comparisons with comparable businesses are often used as a check on such calculations. For purposes of this exercise, aimed at establishing general magnitudes, the number of annual enplanements was judged to be the best general correlate of market value.

Because there have been very few sales (BAA, Burbank) or proposed sales (Albany, Atlanta, Los Angeles International) of commercial airports, there are few points of reference to use in establishing a generic formula. Examination of these five cases, which involve two smaller airports and three very large ones, shows that the values used range from \$30 to \$78 per enplaned passenger (an average value of \$61), with no clear relationship between airport size and dollars/enplaned passenger. Hence, for a first estimation of these 50 airports' possible value, the average valuation factor of \$61 per enplaned passenger was used. (It might be noted in passing that cable television systems are currently valued on the basis of the number of homes in the franchise area, a not-dissimilar method of valuation.)

Revenues of this magnitude would be major windfalls for hard-pressed local governments. Most municipalities have large unmet backlogs of infrastructure projects (road rebuilding and new construction, wastewater treatment, solid-waste disposal, etc.). Most also have large and growing unfunded pension system liabilities. Municipal employees with an eye to their future retirement would have a strong interest in seeing their employer adequately fund their pension system, rather than leaving its future to the vagaries of the political process (when today's office-holders are long gone).

Return of the airport to the tax rolls. Property taxes are the core revenue source for most city and county governments, yet airports--in most cases the largest single user of land in the jurisdiction--are not included on the property tax rolls. While some airports do make certain in lieu payments, those revenues do not come close to what local governments would generate if the airports were privately owned and on the tax rolls. Table 3 presents estimates of the annual property tax revenues which might be obtained from the top 50 airports, valued at the amounts shown in Table 2 and assuming a nominal property tax rate of 1.75% of market value (except in California and Massachusetts). Actual revenues would, of course, depend on the actual effective property tax rate in each community.



TABLE 2  
LARGE AIRPORT MARKET VALUES

RANK BY SIZE	SYMBOL	NAME	1987 ENPLANEMENTS	ESTIMATED MARKET VALUE
1	ORD	Chicago	27,618,295	\$1,684,715,995
2	ATL	Atlanta	24,001,009	\$1,464,061,549
3	LAX	Los Angeles	21,801,305	\$1,329,879,605
4	DFW	Dallas/Ft. Worth	20,974,098	\$1,279,419,978
5	DEN	Denver	16,144,504	\$984,814,744
6	JFK	NY-Kennedy	14,652,734	\$893,816,774
7	SFO	San Francisco	14,566,099	\$888,532,039
8	LGA	NY-LaGuardia	12,049,294	\$735,006,934
9	EUR	Newark	11,798,779	\$719,725,519
10	MIA	Miami	11,786,797	\$718,872,617
11	BOS	Boston	11,589,273	\$706,945,653
12	STL	St. Louis	10,152,163	\$619,281,943
13	DTW	Detroit Metro	9,948,372	\$606,862,892
14	HNL	Honolulu	9,735,344	\$593,868,184
15	MSP	Minneapolis/St. Paul	8,966,394	\$546,950,034
16	PHX	Phoenix	8,911,660	\$543,611,260
17	PIT	Pittsburgh	8,723,284	\$532,120,324
18	LAS	Las Vegas	7,802,162	\$475,931,802
19	PHL	Philadelphia	7,692,304	\$469,230,544
20	DCA	Washington National	7,561,677	\$461,262,297
21	MCO	Orlando	7,506,215	\$457,879,115
22	IAH	Houston Int.	7,399,570	\$451,373,770
23	SEA	Seattle	7,178,491	\$437,887,951
24	CLT	Charlotte	6,472,651	\$394,831,711
25	MEM	Memphis	5,344,763	\$325,847,543
26	IAD	Washington Dulles	5,194,902	\$316,889,022
27	SAN	San Diego	5,059,380	\$308,622,180
28	TPA	Tampa	5,002,812	\$305,171,532
29	SLC	Salt Lake City	4,895,326	\$298,614,886
30	MCI	Kansas City	4,698,252	\$286,593,372
31	BWI	Baltimore	4,635,322	\$282,754,642
32	FLL	Ft. Lauderdale	4,308,602	\$262,824,722
33	HOU	Houston/Hobby	3,935,757	\$240,081,177
34	SJU	San Juan	3,642,766	\$222,208,726
35	CVG	Cincinnati	3,642,684	\$222,203,724
36	MSY	New Orleans	3,484,797	\$212,572,617
37	CLE	Cleveland	3,320,978	\$202,579,658
38	BNA	Nashville	3,178,595	\$193,894,295
39	PDX	Portland	2,870,189	\$175,081,529
40	SJC	San Jose	2,843,698	\$173,465,578
41	MDW	Chicago Midway	2,637,784	\$160,904,824
42	SAT	San Antonio	2,514,604	\$153,390,844
43	DAL	Dallas/Love	2,443,995	\$149,083,695
44	RDU	Raleigh/Durham	2,428,389	\$148,131,729
45	IND	Indianapolis	2,426,168	\$147,996,268
46	BDL	Hartford	2,397,226	\$146,230,786
47	DAY	Dayton	2,381,816	\$145,298,776
48	PBI	West Palm Beach	2,320,353	\$141,541,533
49	OGG	Hawaii	2,276,400	\$138,860,400
50	ONT	Ontario	2,271,842	\$138,582,362
		TOTAL MARKET VALUE		\$23,496,301,714

TABLE 3  
POTENTIAL PROPERTY TAX REVENUE  
FROM LARGE AIRPORTS

RANK BY SIZE	SYMBOL	CITY	ESTIMATED MARKET VALUE	ASSUMED TAX RATE (percent)	ANNUAL PROPERTY TAX PAYMENT
1	ORD	Chicago	\$1,684,715,995	1.75	\$29,482,530
2	ATL	Atlanta	\$1,464,061,549	1.75	\$25,621,077
3	LAX	Los Angeles	\$1,329,879,605	1.00	\$13,298,796
4	DFW	Dallas/Ft.Worth	\$1,279,419,978	1.75	\$22,389,850
5	DEN	Denver	\$984,814,744	1.75	\$17,234,258
6	JFK	NY-Kennedy	\$893,816,774	1.75	\$15,641,794
7	SFO	San Francisco	\$888,532,039	1.00	\$8,885,320
8	LGA	NY-LaGuardia	\$735,006,934	1.75	\$12,862,621
9	EWR	Newark	\$719,725,519	1.75	\$12,595,197
10	MIA	Miami	\$718,872,417	1.75	\$12,580,271
11	BOS	Boston	\$706,945,653	2.50	\$17,673,441
12	STL	St.Louis	\$619,281,943	1.75	\$10,837,434
13	DTW	Detroit Metro	\$606,862,892	1.75	\$10,620,101
14	HNL	Honolulu	\$593,868,184	1.75	\$10,392,693
15	MSP	Minneapolis/St. Paul	\$546,950,034	1.75	\$9,571,626
16	PHX	Phoenix	\$543,611,260	1.75	\$9,513,197
17	PIT	Pittsburgh	\$532,120,324	1.75	\$9,312,106
18	LAS	Las Vegas	\$475,931,882	1.75	\$8,328,808
19	PHL	Philadelphia	\$469,230,544	1.75	\$8,211,535
20	DDA	Washington National	\$461,262,297	1.75	\$8,072,090
21	MCO	Orlando	\$457,879,115	1.75	\$8,012,885
22	IAH	Houston Int.	\$451,373,770	1.75	\$7,899,041
23	SEA	Seattle	\$437,887,951	1.75	\$7,663,039
24	CLT	Charlotte	\$394,831,711	1.75	\$6,909,555
25	MEM	Memphis	\$325,847,543	1.75	\$5,702,332
26	JAD	Washington Dulles	\$316,889,022	1.75	\$5,545,558
27	SAN	San Diego	\$308,622,180	1.00	\$3,086,222
28	TPA	Tampa	\$305,171,532	1.75	\$5,340,502
29	SLC	Salt Lake City	\$298,614,886	1.75	\$5,225,761
30	MCI	Kansas City	\$286,593,372	1.75	\$5,015,384
31	BWI	Baltimore	\$282,754,642	1.75	\$4,948,206
32	FLL	Ft. Lauderdale	\$262,824,722	1.75	\$4,599,433
33	HOU	Houston/Hobby	\$240,081,177	1.75	\$4,201,421
34	SJU	San Juan	\$222,208,726	1.75	\$3,888,653
35	CVG	Cincinnati	\$222,203,724	1.75	\$3,888,565
36	MSY	New Orleans	\$212,572,617	1.75	\$3,720,021
37	CLE	Cleveland	\$202,579,658	1.75	\$3,545,144
38	BNA	Nashville	\$193,894,295	1.75	\$3,393,150
39	PDX	Portland	\$175,081,529	1.75	\$3,063,927
40	SJC	San Jose	\$173,465,578	1.00	\$1,734,656
41	MDW	Chicago Midway	\$160,904,824	1.75	\$2,815,834
42	SAT	San Antonio	\$153,390,844	1.75	\$2,684,340
43	DAL	Dallas/Love	\$149,083,695	1.75	\$2,608,965
44	RDW	Raleigh/Durham	\$148,131,729	1.75	\$2,592,305
45	IND	Indianapolis	\$147,996,248	1.75	\$2,589,934
46	BDL	Hartford	\$146,230,786	1.75	\$2,559,039
47	DAY	Dayton	\$145,290,776	1.75	\$2,542,589
48	PBI	West Palm Beach	\$141,541,533	1.75	\$2,476,977
49	GGG	Haul	\$138,860,400	1.75	\$2,430,057
50	ONT	Ontario	\$138,582,362	1.00	\$1,385,824

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In contrast with the status quo, in which municipalities "own" their airports but cannot derive net revenues from them, selling the airports would convert them into net revenue generators for local governments, year after year, on into the future.

**Dynamic revenue gains from property development.** Generally speaking, government airport operators see themselves as being in the airport business, period. Because they are not supposed to make a profit, they concentrate on providing airport services on a break-even basis. By contrast, those companies seeking to enter the airport business view airports as property-development opportunities. By bringing together compatible uses, on and adjacent to the airport property, they hope to maximize the return on their investment.

In the Albany privatization, the consortium (which includes a local firm, British American, experienced in property development) proposed investing \$69 million in land improvements on the airport property (in addition to the terminal and other airport buildings, per se). This would include a 250-room hotel, a warehouse, and a service center. In addition, British American proposed spend \$75 million to develop a commercial complex on 75 acres adjacent to the airport, including mixed-use offices and retail stores.

Similarly, the driving force behind the the proposed quasi-privatization of the Peoria Airport is land development. The proposal would increase the size of the airport complex from 2,400 to 3,400 acres (about half the size of Chicago's O'Hare). While providing additional buffer land for noise abatement and approach compatibility, the main purpose of the added land is to maximize value by developing profitable uses compatible with the airport: warehousing, transshipping, aircraft overhaul, hotel and conference space, office space, retail, etc.

Most commercial airports are underutilizing their land, because value-maximization is not part of their current charter. Under private ownership, it would be. And this would result in major increases in property value (and job creation), both on and adjacent to the airport property. These revenue flows are difficult to estimate, but they make the (static) property value estimates in Table 3 extremely conservative.

### **C. National Benefits from Airport Privatization**

Airline deregulation unleashed unprecedented growth in domestic air travel, as prices dropped in real terms and flying became routine for a much larger fraction of the population. The upcoming economic liberalization of Europe, post-1992, and the rapid growth of the Asia-Pacific market, will produce further large increases in air travel to and from this country. Major increases in airport capacity will be needed in the next two decades, not only by increasing the capacity of existing airports but also by building entire new airports.

There is strong interest by private capital in getting into the airport business. Overseas, investors snapped up BAA's shares and will likely do the same for those of the Copenhagen airport. Private capital is going into the new Brussels airport, Japan's new offshore Kansai airport, and new airports being planned for Hong Kong and Macao. It was not coincidence that it was a leading investment banking firm, Merrill Lynch Capital Markets, that held discussions with the city of Atlanta in 1988 regarding the possible sale of Hartsfield International Airport. The investment banking community--including major firms in London, Zurich, and Tokyo, as well as New York--views airports as potentially lucrative investments. At a time when the Congress has difficulty keeping itself from raiding the Airport Trust Fund, it would be foolhardy to ignore the potential of bringing private capital into the airport business.

In the near term, that means opening the door to privatization of existing commercial airports. For the longer term, it will mean devising federal policies to encourage the creation of new

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airports as business ventures. (That subject will be addressed in a subsequent Reason Foundation policy study.) Broadly speaking, a national policy to foster airport privatization offers a way to meet our national airport capacity needs without busting the federal budget.

Airport privatization would also mean new revenues for the federal government. Just the top 50 commercial airports, operating as private enterprises and earning a nominal 10% annual return on assets would generate profits of \$2.35 billion per year. At the average effective federal corporate income tax rate of 26% [20], there would be \$611 million in additional federal tax revenues per year from these companies.

Critics of airport privatization have said that selling airports to private enterprise would frustrate the goal of a "national system" of airports. Yet given the obvious mismatch between this country's need for additional airport capacity and the federal resources available to meet that needs, as well as the lack of progress on as modest a goal as spending all the money in the Aviation Trust Fund, such criticism must be taken with a grain of salt.

A "national system" of airports need not mean one whose spending decisions are made in Washington, DC. The first requirement of such a system is that it meet the need for adequate capacity--something the present system clearly is not doing. If privatization of airports offers the nation a way to meet that need, it must be seriously considered. And that is precisely what privatization offers.

The federal government will continue to have an important role to play in ensuring a national airport system, even when it is no longer attempting to central plan airport investment from Washington. A national system means one in which the basic rules of the game are the same nationwide, in furtherance of free-flowing interstate commerce.

This clearly requires strong, consistent safety regulation and enforcement by the FAA. Airport air traffic controllers would still be licensed by the FAA, as are pilots and mechanics who work for (privately owned) airlines. The FAA would still test and inspect the airport-owned radars and landing aids, define and enforce (via Federal Air Regulations) the rules of the road for the airways, and carry out other needed safety-related functions.

The federal government could also attach various conditions to a municipality's sale of its airport, so as to ensure continued aviation use and nondiscriminatory access under market pricing. These conditions would be justified in view of the federal government's previous capital investment via federal airport grants.

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## V. RECOMMENDATIONS FOR A NATIONAL POLICY

The federal government can play the key role in channeling greater resources into U.S. airports--without any increase in the federal budget. It can do this by fostering the privatization of this country's large commercial airports (large and medium hubs). Specific policies for doing so are set forth in the following paragraphs.

### A. Overall Privatization Policy

A policy encouraging privatization would permit any large or medium hub to opt out of the present funding system, converting the airport to a private corporation. The present state, county, municipal, or public authority owner would sell the airport using any of several standard methods (sale to a consortium, sale via public stock offering, worker/management buyout, or some combination). The federal government would offer the following to any airport opting for privatization:

- The right to charge nondiscriminatory market-based landing fees (including peak-hour differentials);
- The right to charge per-passenger fees:
- Reduction in the 3% ticket tax to 4% for passengers originating at the airport.
- Divestiture of the control tower and landing aids to airport ownership, with the controller workforce becoming employees of the airport;
- Ownership of landing/take-off slots at that airport, with the right to lease them to users on a market-price basis;
- The municipality's right to use the one-time sales proceeds for its general-fund budget.

In turn, the airport would give up any and all access to federal airport grants, both entitlements based on enplanements and discretionary grants. The only condition it would have to agree to is that the facility must continue to be used as a public-access airport for its entire useful life. Otherwise, the airport would be relieved of having to meet the numerous conditions and regulations required of Aviation Trust Fund grantees. The airport would, of course, remain fully subject to FAA safety regulation, as it is at present.

Because it would be voluntary, this policy would be consistent with American principles of federalism. The federal government would not require any airport to opt for privatized status; only those which desired the new freedoms and responsibilities would choose this new option. The policy also provides wide scope for experimentation with different types and mixes of revenue sources for the privatized airports. Over time, the aviation community would gain considerable knowledge about which types of fees and charges work best.

Privatization would foster investments in increased capacity at the 50 large and medium hub airports which serve the lion's share of all airline flights and passengers--precisely the airports which are, or soon will be, congested bottlenecks in the national aviation system. And it would do so entirely by user funding.

The federal government would gain a new source of corporate income tax revenue from the new airport companies. In addition, the aim of spurring more airline competition at hubs would be served more effectively if airlines had to deal with a private airport firm, rather than a public agency.

Congress may not address privatization in the near term. Yet DOT will probably be faced with more cases (such as Albany) where municipalities wish to sell or lease their airports to private firms. DOT could significantly encourage such sales by excluding from the definition of

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"revenues generated on the airport," the one-time revenue from such sales. This would permit the municipality to apply the sales revenue to its general-fund budget. Such a provision would be a major incentive to airport privatization.

### **B. Ensuring Competition**

To ensure that privatization fosters increased competition and does not lead to either airline or airport monopoly problems, several additional policies should be adopted. First, ownership of airports by airlines should be restricted or prohibited, so as to ensure arms-length dealings between airport companies and airline tenants. In metropolitan areas with more than one air-carrier airport (e.g., Chicago, Dallas, Houston, Los Angeles, New York, Washington), no private firm should be permitted to own more than one of the airports.

Price regulation, by contrast, will probably not be needed, even in single-airport cities. Because airlines will be free to reduce or eliminate service to an airport whose charges are out of line, they will be in a strong bargaining position to resist unreasonable charges. Passengers can also resist being exploited by monopolistic pricing. If airport parking rates are exorbitant, they can turn to off-airport parking lots and garages. And if airport gift shops and coffee shops charge exorbitant prices, passengers will simply not patronize them. They are not captive customers, in the sense that electricity or local telephone customers are captive of the monopoly provider of an essential service.

In any case where price regulation should be found necessary, it should be imposed by DOI rather than state public utility commissions. Modern British-type price caps in relation to inflation (RPI minus X) should be used, rather than traditional U.S. rate-of-return regulation (which tends to promote excessive levels of capital investment).

### **C. Leveling the Investment Playing Field**

In order to encourage private investment in airport capacity, the present disparity between the interest rates which public and private airports must pay on revenue bonds should be removed. Currently, even though tax-exempt revenue bonds for airports are subject to an annual state-by-state cap, their tax-exempt status results in significant interest-rate savings compared with an otherwise identical taxable airport revenue bond. There is little justification for airport bonds to be tax-exempt in the first place. The main beneficiaries of this tax exemption are profit-making airlines; in effect, the availability of tax-exempt bonds constitutes a form of federal subsidy to the airlines (in contrast, say, to the railroads which must pay for their own infrastructure using taxable debt and equity capital). Thus, removing the tax exemption for all airport bonds (or, alternatively, making all airport revenue bonds tax-exempt, regardless of the issuer) would significantly level the playing field between public and private airports.

### **ABOUT THE AUTHOR**

Robert W. Poole, Jr. holds B.S. and M.S. degrees in engineering from MIT. He has served as a White House consultant on privatization of air traffic control and postal services, and advised the President's Commission on Privatization on aviation privatization issues. He serves as president of the Reason Foundation. Reason Foundation research fellow William Eggers provided extensive research support for this paper.

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