Statement of Faye Malarkey
Vice President, Legislative Affairs
Regional Airline Association

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Transportation and Infrastructure Committee's
Subcommittee on Aviation

hearing on:

The Essential Air Service Program and the
Small Community Air Service Development Program

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Chairman Costello, Representative Petri, and Members of the Subcommittee, thank you for the opportunity to testify before you today. I am pleased to join today's distinguished panel in order to discuss the topic of enhancing scheduled commercial air service to small and rural communities.

My name is Faye Malarkey and I am Vice President for Legislative Affairs with the Regional Airline Association (RAA). Although I have been working on this issue alongside Members of this Committee, as well as my colleagues on the other panels, for almost 10 years, today marks the first time I have the honor of providing formal testimony before this Subcommittee.

On behalf of the Regional Airline Association and our member airlines, I thank you for holding this timely hearing.

Background

RAA represents 41 U.S. regional airlines transporting 97 percent of all regional airline passengers. Our member airlines operate 9 to 68-seat turboprop aircraft and 30 to 108-seat regional jets and link together more than 600 communities in the United States.

At more than 70 percent of these communities, regional airlines provide the only source of scheduled airline service. Nowhere is the importance of regional airline service more apparent than at the more than 140 rural communities across the country that receive scheduled air service through the Department of Transportation's Essential Air Service Program (EAS).

The smallest airports, such as those with between one and three daily departures, have seen a 21 percent decline in daily departures between September 2001 and September 2006. Thirteen of these airports have lost service altogether. Airports with between three and six daily flights in September 2001 have experienced a 33 percent decline in departures with eight such airports losing service altogether. Because of increasing costs and continuing financial pressures in the post 9/11 aviation industry, at least 40 additional communities have been forced onto the EAS roles and 17 EAS communities have been dropped from the program altogether in the past five years.

As Members of this Subcommittee know, EAS was initially created as part of the Airline Deregulation Act of 1978. The program has been in effect each year since. Ten years after the program's original inception, Congress recognized that the free market alone could not be relied upon maintain air service to all small communities. At this time, Congress reauthorized the program for an additional 10 years. Congress later enacted the "Rural Survival Act of 1996," which removed the sunset provision governing EAS and codified a permanent funding stream for the program.

With the advent of new highways and increased highway speed limits, Congress has put in place more stringent distance criteria (currently 70 highway miles or more from the nearest medium or large hub airport, 55 highway miles or more from the nearest small hub airport, or 45 highway miles or more from the nearest non-hub airport with 100 or more daily passenger enplanements) and a per passenger subsidy cap of $200, enacted in 1990, for communities within 210 miles of a large or medium hub airport.

In 1999, the Department of Transportation issued several service termination orders, triggering broad opposition from communities and air carriers, which highlighted the need for a sufficient and stable funding stream for EAS. Congress moved to increase funding for the program, and raised EAS funding to $113 million in Fiscal Year 2003 as part of the Century of Aviation Reauthorization Act. The law included several additional provisions aimed at reforming the EAS program, including a community cost-sharing pilot program. This proposal was met with so much opposition that its implementation was expressly prohibited in subsequent Appropriations.

During the 109th Congress, Appropriations bills in both Chambers slated $117 million for the program, but because the 109th Congress adjourned without passing a DOT Appropriations package for Fiscal Year 2007, the program is now being funded at 2006 enacted levels.

Congress included a provision in the Deficit Reduction Act of 2005 to set aside $15 million from telecom spectrum sales to fund the EAS program in Fiscal Years 2007 and 2008. Unfortunately, the provision contained a trigger mechanism, permitting the release of funds only if Congress funded the program at a minimum of $110 million. Because Congress simply extended FY06 funding levels for the current fiscal year, the total appropriation of $109.4 million falls $0.6 million short of the $110 million needed to trigger the release of additional funds. As a result, the additional $15 million in funding has not been released to date.

Department of Transportation and Federal Aviation Administration Proposals

The proposal contained in the FAA's own reauthorization bill this year would severely cut and potentially dismantle the EAS program as funding would fall by $59 million from current enacted levels, effectively forcing out a third or more of the communities that now use the program. The proposal further caps EAS subsidies at current levels and prohibits the addition of new EAS points for communities that lose air service in the future, telling residents of these communities that convenient, reliable air service is a luxury, and one they can't have. For the others, DOT would set up a tiered system to grant reduced subsidies to communities in descending order of distance from nearby hub airports, starting in Alaska and continuing until the funding runs out, which is sure to happen long before DOT's obligation to EAS communities has been met.

If enacted, this proposal would jeopardize rural air service in an unprecedented way because it fails to reflect the fact that, of 140 current EAS communities, 85 -- 36 in Alaska alone -- are further than 210 miles away from a medium or large hub airport.

Dozens more are further than 150 miles away from the nearest medium or large hub airport. Yet, under the DOT's proposal, even many remote communities would lose air service as the funding level proposed by DOT is simply too low to continue the program in any meaningful way.

While we have deep respect for our colleagues at FAA and DOT, it seems unlikely that such proposals have been offered with an eye toward enhancing and improving the program. Rather, these proposals seem designed to severely cut or even eliminate the program altogether.

We share with this Committee an understanding of the critical role air service plays in driving the economies of smaller communities and request the Committee's assistance in helping us protect rural communities against cuts that would undermine the EAS program. We also greatly appreciate the initiative DOT has taken, recently, in reaching out to the industry to solicit ideas on EAS reform. We stand ready to work with DOT and with this Committee to reach a shared goal for meaningful EAS reform.

Congress promised small communities, back in 1978, that deregulation would not leave them behind; rather, communities receiving scheduled air service before deregulation would continue to receive scheduled air service after deregulation. The vehicle for this promise has been EAS, and while we recognize the usefulness of reform, we urge Congress to reject proposals that significantly cut, eliminate, or undermine this important program.

Carrier Costs and Real-Time Rate Indexing

One of the greatest factors contributing to diminishing small community air service is the continuous and staggering affect of fuel cost increases. Turboprop aircraft are among the most fuel efficient aircraft for short-haul routes and, like our major airline counterparts, regional airlines have sought to minimize fuel burn by tankering fuel, lowering cruise speeds, safely altering approach procedures, and reducing onboard weight. We are making every effort to manage escalating fuel costs with an eye toward conservation. Nonetheless, fuel is now the highest cost for many regional airlines.

As part of the competitive EAS application process, carriers negotiate in good faith with DOT on subsidy rates that remain in effect for two years. In doing so, EAS carriers must project revenues and costs over this same two-year timeframe – no easy task in today's volatile cost environment. In cases of unexpected cost increases, EAS carriers lack a mechanism to renegotiate rates and must instead enter into the unpalatable process of filing 90 day service termination notices in order to begin the convoluted process of seeking rates that cover increased costs. This inevitably causes ill-will between airline and community and fosters a sense of unreliability that undermines community trust in and use of the air service.

Furthermore, one of the fundamental tenets of the EAS program held that no carrier should be expected to serve any market at a loss. Yet, in cases of unexpected cost increases, carriers are unable to provoke rate changes without filing such service termination notices, after which each carrier must continue to provide the service, at a loss, for 180 days while DOT undertakes the competitive bidding process.

The impact on rural air service is significant. Take the case of Merced, CA. While the carrier involved with the market engaged in rigorous cost savings and was able to initially double the traffic forecast in its original EAS proposal, escalating fuel costs ultimately caused the carrier to file 90 day notices at Merced as well as Visalia, CA and Ely, NV, noting:

> "Scenic's need to terminate service at [Merced / Visalia / Ely] stems primarily from fuel cost escalations that have undermined the economic viability of the carrier's EAS operations. As a consequence, Scenic has decided to refocus its resources on its historical aerial sightseeing operations and discontinue scheduled-service operations."

In 2005, Great Lakes Aviation experienced fuel cost increases of 21 percent, even though its fuel consumption was down 11 percent due to a reduction in scheduled flights. In fact, Great Lakes' average fuel cost per gallon increased almost 37 percent in a single year, costing 1.7 additional cents per Available Seat Mile (ASM).

In recent weeks, crude oil has climbed to over $60 dollars a barrel. To put these statistics into perspective, consider this: EAS contracts have a two-year lifespan. A winning carrier who negotiated a competitive contract one year ago would have based cost projections on then-current fuel rates of $1.80 per gallon. That same carrier would now be providing the service with fuel costs at $2.00 per gallon and climbing. (Recently, Federal Reserve Chairman Ben Bernanke remarked that the possibility of fuel costs reaching $3 a gallon this year is "not out of the question.") Because EAS carriers are strictly limited to five percent profit margins, climbing fuel costs frequently turn once-profitable routes into loss-generating routes.

Because one of the fundamental tenets of EAS holds that no carrier should be forced to serve any market at a loss, Congress addressed the rate-adjustment issue twice. In Section 402 of Vision 100, the Century of Aviation Reauthorization Act, Congress affording DOT a rate-indexing mechanism to make real-time adjustments during periods of significantly increased carrier costs. In order to prevent deliberate cost underestimation, Congress required carriers to demonstrate "significant increases," defined as a 10 percent increase in unit costs persisting for two or more consecutive months, to trigger the adjustment.

There is little doubt that situations like the one with Scenic Airlines and Merced / Visalia / Ely could have been prevented had Section 402 been implemented to curb the grave financial consequences that EAS carriers are experiencing as a result of serving markets at a loss. Unfortunately, DOT has been unwilling to implement the program to date, citing a lack of funds.

In response, Congress included a provision in the Deficit Reduction Act of 2005 appropriating an additional $15 million to offset costs associated with rate adjustments. Unfortunately, because of the unforeseen Appropriations shortfall this year, the trigger mechanism detailed earlier in this briefing has not been met and the funds have not been released.

RAA therefore respectfully asks Congress to include language in the expected FAA bill to *require* DOT to make real-time rate adjustments and asks that Congress reverse the requirement of a $110 million trigger for release of additional funding for Fiscal Years 07 and 08.

RAA stands ready to help Congress enact EAS program reforms as the next FAA Reauthorization takes place. We understand that a rewrite of the eligibility criteria may be necessary as some of the rules set nearly three decades ago may no longer apply. These decisions should be based on rational factors and not a funding crisis at DOT.

RAA further asks that Congress carefully examine all evidence suggesting the program is not facing a funding shortfall. The demonstrability of funding needs and expenditures related to the EAS program is closely tied to management of the program. DOT should not be allowed to cut service levels or eliminate points in order to lower programmatic expenditures without reinvesting in the program. In doing so, DOT trades a funding problem for a service commitment problem – one that carriers can do little to reverse.

Eliminated service points generate excess cash in the EAS coffers, which suggest that the program is over-funded; in fact, these funds should instead be reinvested in the program to raise service levels at more viable routes, thereby allowing passengers to best utilize service that has been granted. In order to fully explore these issues, RAA requests that Congress require an audit on unspent, obligated EAS funds currently retained on the EAS balance sheets.

As Congress considers potential eligibility criteria changes, we also ask that the same standard is applied. Reforms to the program should be aimed at enhancing the program and protecting rural air service; not gutting the program. Therefore, we ask that any service reductions resulting from EAS reform be revenue neutral. Subsidies recovered from communities losing eligibility should not be diverted from the EAS program but should instead be reinvested in the program. Given the correlation between increased frequency and increased enplanements, such a reinvestment could serve to help some communities reduce or eliminate subsidy reliance altogether.

Date Certain for Market Exit

Part of the nature of the Essential Air Service program, as you know, is that carriers compete rigorously for contracts. Even in cases where an incumbent carrier desires to continue serving a given market, DOT has the right to select another carrier. In cases where DOT awards service to a new carrier, RAA believes DOT should be required to give the incumbent carrier a date certain when it may exit the market, without exception.

The current practice, where DOT holds the carrier in markets in 30 day increments, is untenable. This practice means a carrier cannot sell tickets in the EAS market beyond 30 days, nor can it make plans to utilize its aircraft elsewhere. We urge Congress to end this unfair situation by mandating that DOT adopt a date certain component for incumbent carrier market exits when it selects an alternate carrier to serve the market.

DOT Term Length Upgrade

As you know, DOT contracts have a two-year lifespan. Post 9/11, DOT was fortunate that carriers possessed excess aircraft inventory sufficient to facilitate competitive bidding on new EAS routes. With more and more turboprop aircraft being sold overseas, there are fewer aircraft available in the United States for this type of service.

Unfortunately, airlines' ability to commit aircraft in a diminishing market has likewise grown more difficult. Aircraft financing models are ill-suited to short, two year-year commitments. In fact, one reason there are so few new-entrant EAS carriers, may be attributed to the lack of financing for aircraft with short-term commitment levels.

By upgrading the EAS contract terms to four or five-year service commitments, existing carriers would be better able to renew current contracts, a significant barrier to market-entry would be removed, and all carriers would better able to finance aircraft for longer-term obligations.

Smaller Aircraft and Very Light Jets

Both DOT and the Government Accountability Office (GAO) have recently discussed the use of Very Light Jets (VLJs) as the rising operating costs of current EAS carriers have translated to higher EAS program costs. Ironically, the rising costs in question have occurred as a result of compliance with the single-level-of safety standards imposed on this part of the industry in 1997 when the FAA moved smaller regional carriers to FAR Part 121. While RAA does not advocate a return to separate regulatory standards for 19 seat aircraft, the government should not be allowed to replace existing Part 121 carriers, who have diligently complied with the regulatory change at great cost, with new-entrant VLJs operating under the very same regulations the Agency formerly deemed inadequate.

Beyond the regulatory perspective, the business models of those smaller aircraft remain unproven. More questions than answers remain about how VLJs will operate. Will they feature reservations systems? Will they abandon the "on demand" model and simply become scheduled service on a very small airplane? Who is held responsible if a government-subsidized air taxi fails to fulfill a trip? Would VLJs be subject to regulations governing carriage of disabled passengers? Would the government be willing to scrutinize and, if necessary, enforce VLJ compliance with industry standards on lost-baggage and overbooked flights?

Additionally, the VLJ business models that do exist promise direct, non-stop service to destinations that would bypass the hub and spoke system. They would therefore fail to connect passengers to the existing air transportation system in favor of limited service. The fares for VLJs are also another great unknown, but most advocates pushing VLJ technology acknowledge they are "fairly expensive." Some communities eager to see VLJ service as an air service solution admit the on demand aircraft would ideally supplement, but not replace, EAS service.

We strongly caution the Congress against advancing this unproven technology as a solution to EAS shortfalls. The Congressional commitment to rural communities during deregulation was a continuation of *scheduled* air service. It is inappropriate to place the burden on passengers and communities to secure air service through expensive, untested, and potentially unreliable sources. Instead, we urge Congress to fully fund the program and to keep careful watch on the policies that are forcing communities into (and out of) the EAS program.

FAA Reauthorization and User Fee Proposals

The FAA proposal, which treats commercial airline passengers differently based on size or type of aircraft, discriminates against passengers from smaller communities. Further, the proposal undermines the notion of a national system of commercial aviation. Regional airlines provide 14,000 flights daily. To ignore the crucial service regional airlines provide in smaller communities by dismissing regional airline flights and passengers as a mere "blip" on a radar screen represents more than an oversimplification. Instead, such proposals fail to treat passengers equally, regardless of the point at which they access the system or how many passengers are seated onboard alongside them.

A recent press release from the FAA claimed that our belief that FAA's proposal would jeopardize service to small communities was "a myth." Let me tell you that the FAA user fee scenario, if enacted as is, would certainly and undeniably increase regional airline costs and would certainly and undeniably reduce service to smaller communities.

The FAA's proposal could also directly affect the EAS program by blocking service to congested airports -- carriers simply cannot amortize the cost of increased fees over the type of aircraft deployed along EAS routes.

We pledge to work together with Congress on our common goal of modernization but ask that you ensure regional airlines – and their passengers in medium and small communities throughout the United States – are not disenfranchised in the process.

Conclusion

Mr. Chairman, thank you for the opportunity to testify on this important issue today. I look forward to responding to your questions at the conclusion of the panel.

The Regional Airline Association represents U.S. regional airlines, and the manufacturers of products and services that support the industry, before the Congress, DOT, FAA and other federal agencies. Founded in 1975, RAA also provides a wide array of technical and promotional services to regional airlines. The association's member airlines transport 97 percent of total regional airline industry passengers. RAA engaged BACK Aviation, an aviation consulting firm, to compile the data. Data should be sourced to RAA and BACK Aviation.