Statement of the Honorable D.J. Gribbin
General Counsel, U.S. Department of Transportation
Before the
U.S. House of Representatives
Committee on Transportation and Infrastructure
Subcommittee on Aviation
Concerning
Aviation Congestion Management
June 18, 2008

Introduction

Mr. Chairman and members of the Subcommittee, thank you for the opportunity to testify again on the Department of Transportation's (DOT) continuing efforts to address aviation congestion.

Status of the industry

Before I go into detail about the DOT's efforts to address congestion, I want to take a moment to talk about the particularly challenging environment currently facing the airlines. As my fellow panelists well know, record oil prices, a slowing economy, and increased competition are just a few factors that have created a number of significant challenges for airlines – challenges that certainly will change the face of the aviation industry in the years to come.

To meet these challenges, many carriers are raising fares, streamlining operations, and reducing service. It is possible that some of these measures will result in reduced congestion – however, so far we have yet to see widespread evidence of carriers pulling out of the busiest (and most congested) airports. Although, Continental announced just last week that they are eliminating service to 15 communities, it is likely that the busiest and most congested airports will not see an overall reduction in service – and even if there is a reduction, history tells us that the aviation industry is very cyclical and that service will return to – and exceed – the record levels we saw last year.

In 2007, the aviation industry recorded the second worst year for delays since 1995; 27% of flights were delayed or cancelled in 2007. Both the frequency and the severity of ground delays were unprecedented. The costs of delays are huge – the Senate Joint Economic Committee estimates that last year flight delays alone cost passengers, airlines, and the U.S. economy over $40 billion. Additionally, the Travel Industry Association estimates that air travelers avoided over 41 million trips last year – leading to lost revenues and taxes of over $26 billion.

The cost of delays and congestion to the U.S. economy is huge and that is why, even if carriers reduce flights this summer enough to reduce congestion, we still must do something to fix the problems that caused last summer's horrible delays. We simply cannot wait until there is another summer of record delays before we do something to fix the system. That is why the Department will continue working on its initiatives to address congestion and introduce competition at capped airports.

LaGuardia/JFK/Newark Background:

As you all know, the Department recently published notices of proposed rules intended to manage congestion at LaGuardia Airport (LaGuardia), John F. Kennedy International Airport (JFK), and Newark Liberty International Airport (Newark). We believe these proposals will ultimately provide travelers with more reliable service while maintaining competition among the many carriers in a vibrant New York market.

Congestion at these three New York airports is not a new phenomenon. Since 1969, the High Density Rule (HDR) has effectively capped LaGuardia to a limited number of operations per hour and capped JFK during its peak hours. Although Newark was once subject to the HDR, the FAA suspended its application in 1970 due to the fact that capacity was meeting demand. In recent years, however, operations have bogged down to the point where Newark is now one of the most delay-prone airports in the country. Current and anticipated demand during peak hours at all three airports approaches or exceeds runway capacity, causing volume-related delays, which can be aggravated by weather or other operating conditions. Operational improvements have not increased the capacity of the New York area to a point where the unconstrained demand for air service can be met without excessive congestion. Therefore, for now, all three airports are capped.

Straight caps without some mechanism to ensure an efficient allocation of scarce slot resources is economically inefficient and, therefore, not our preferred option. Our preference is to see airports address their challenges locally through implementation of capacity enhancing projects or procedures, whenever possible. However, the federal government will be involved once a congested airport impacts the rest of the national airspace. In this case, New York air congestion causes delays throughout the U.S., so the federal government cannot ignore the problem. Given the urgent need for action, caps were necessary at the New York City area airports.

When we consider economic regulatory issues, the Department has a statutory obligation to place maximum reliance on competitive market forces and on actual and potential

competition. We know, however, that caps hinder the ability of air carriers to initiate or expand service at capacity constrained airports. Therefore, when seeking a solution to the aviation congestion issues that we currently face in the New York area, the Department must act to both promote competition by permitting access to new entrants, and to recognize the long-term investments in airports made by existing carriers. We do not believe that a simple imposition of caps without some mechanism to preserve competitive market forces benefits aviation consumers or the airlines.

With this in mind, we have set forth proposals for the New York area airports that we believe would reduce congestion the smartest way—by using market incentives to assist in the efficient allocation of airspace. Although market-based mechanisms are the most effective way to allocate scarce resources—like slots—we have taken a very conservative approach to introducing these mechanisms with this proposal. The vast majority of hourly operations at the airport, as much as 90 percent or more, would be "grandfathered" and leased to the existing operators for non-monetary consideration. The market-based aspect of our proposal involves auctioning off leases for only a limited number of the remaining slots.

Are there alternatives to caps and auctions?

Expanded Capacity

Some have incorrectly suggested that expanding capacity should be the only government response to congestion in New York City and around the country. This view largely ignores the tremendous short-term opportunities to utilize existing capacity more efficiently. It also ignores the physical, economic, and political constraints on capacity expansion in many parts of the U.S. aviation system.

The Department shares the view that expanded capacity is a critical component of the long-term solution to relieve congestion and get travelers to their destinations on time and in a humane fashion. We are intensely focused on such solutions, both at the FAA with implementation of the Next Generation Air Transportation System (NextGen) and at the Department level. The FAA is hard at work bringing new technology and techniques on-line to unsnarl air traffic delays, and we appreciate the funding Congress has appropriated for these purposes. In recognition of these critical enhancements, the President's FY 2009 Budget Request would more than triple the investment in NextGen technology – providing $688 million for key research and technology to help meet the nation's rapidly growing demand for air travel, including the transformation from radar-based to satellite-based air traffic systems.

The FAA will begin rolling out several elements of the NextGen system this summer. This rollout will include the national debut of Automatic Dependent Surveillance-Broadcast (ADS-B) technology in Florida.

The FAA has chosen Miami as the key site for the installation and testing of Traffic Information Services – Broadcast (TIS-B) and Flight Information Services – Broadcast (FIS-B). These broadcast services are the transmission of weather and traffic information to the cockpit of properly equipped aircraft. In order to provide the services in roughly the southern half of the state, the contractor, ITT will install and test eleven ground stations in this area, including five at airports (Lakeland Linder Regional, Dade-Collier, Florida Keys Marathon Airport, Boca Raton Airport, and Sebastian Municipal).

The ITT installed equipment is currently undergoing a Service Acceptance Test (SAT) which began in May. In November 2008, the agency expects to commission (the FAA calls this an In-Service Decision or ISD) these broadcast services (TIS-B and FIS-B). Following the successful completion of ISD, the FAA can exercise an option in the ITT contract to deploy the services nationwide

The transition to ADS-B technology will allow the nation's air traffic control system to change from one that relies on radar technology to a system that uses precise location data from a global satellite network. Over the next few years, the FAA will also install and test ADS-B for use in Air Traffic Control Separation Services. The key sites for this initiative are Louisville, Philadelphia, the Gulf of Mexico, and Juneau. The FAA plans to commission the ADS-B services in September 2010 and complete a nationwide rollout by 2013.

The FAA also recently completed stage 1 implementation of its Airspace Redesign Project for the New York, New Jersey, Philadelphia area. The goal of the Airspace Redesign Project is to enhance the efficiency and reliability of the airspace structure and the air-traffic control system for pilots, airlines and the traveling public. The project modernizes the structure of the air traffic environment in an environmentally responsible manner, while laying the foundation for NextGen. Moreover, it will help to accommodate growth while enhancing safety and reducing delays. While airspace redesign will provide greater efficiencies and some congestion relief, it is not a complete solution.

The Department looks to increase capacity both in the air and on the ground whenever possible. Our support for expansion of O'Hare International Airport is one concrete example. The fruits of these efforts became clear on Monday when the FAA announced that it would allow the flight caps put in place at O'Hare in 2004 to expire because of the

additional capacity the airport will gain from its new runway. Capacity increases must be part of the solution, particularly since we expect demand for air travel to resume its robust growth over the coming decade, despite the current temporary pause due to economic conditions. This is especially true in the nation's busiest metropolitan areas. However, capacity increases, both physical and operational, often take a long time to implement and may be limited in scope. Sometimes physical capacity cannot be expanded, such as at LaGuardia Airport. Operational improvements can help to address congestion, but sometimes they cannot provide enough capacity to meet demand. For example, in New York, even with the implementation of all the operational improvements initially suggested by the Air Transport Association (ATA) and the Port Authority, congestion was expected to double this year, assuming the FAA took no further action and the airlines moved forward with planned increases in their schedules.

There are additional solutions. Basically, we have a choice between two fundamentally different approaches – administrative remedies and market-based solutions. We believe that outdated government policies relying on administrative remedies alone have led to an inefficient allocation of the airspace, and that moving towards a system that includes market-based solutions will reduce these inefficiencies and contribute to an improved flying experience for air travelers.

Administrative Allocation

Instituting administrative remedies, such as caps, is an effective, but not efficient way to reduce delays. Limiting the number of flights into an airport will reduce congestion at that airport. The Department decided to institute a short-term cap at JFK and Newark airports because something needed to be done to avoid a repeat of the flight delays that we experienced last summer. However, caps are not the best solution for improving travel options for passengers.

Airlines are often enthusiastic in their support of caps at an airport they already serve. When a cap is established, incumbents are protected because they typically maintain their market share and the potential for new competition is diminished. The incumbent airlines' support for such a policy makes sense, because limited competition makes them more profitable and protects them from new entrants that might want to compete by offering lower fares.

Although caps protect existing airline business, they also prevent airlines from adding capacity at an airport unless they are able to obtain a slot from a competitor. As a result, one of the best-known problems with slots is that they encourage airlines to "babysit" slots, i.e., underutilize the slot by flying multiple small aircraft into an airport to

maximize the number of slots an airline can occupy at the lowest possible cost.[1] As a result, slots do not always go to those who value them the most and who will use the capacity in the most efficient manner.

This limitation on capacity and competition naturally leads to fare increases at an airport, because it creates a scarce commodity, and passengers pay a premium for that commodity.

If caps are not the long-term answer, then the question arises – what is the solution?

Market-Based Remedies

Alfred Kahn, an airline economist and former Chairman of the Civil Aeronautics Board, said: "Whenever competition is feasible, it is, for all its imperfections, superior to regulation as a means of serving the public interest." Secretary Peters echoed that sentiment when she said: "Our preference is to find a way to let market incentives do the job, and not to return to the days of government-regulated flights and limited competition." Although the Department instituted caps as a short-term measure, we continue to explore market-based remedies as a long-term solution to congestion.

It is clear that the current system does not allocate airspace capacity efficiently. Solving that problem, however, should not entail government picking "winners and losers," particularly when, as currently structured, everyone involved in air travel feels like they are the loser—both those getting terrible service and those getting blamed for providing terrible service.

Market-based pricing has been demonstrated time and again as the most effective way to allocate a scarce resource that is in high demand. Space in a movie theater, use of cell phone infrastructure, or flights during certain times to certain destinations are all examples that illustrate that such pricing works. Pricing can balance demand with available capacity, resulting in less congestion and more reliable schedules. Also, pricing sends better signals as to where the system needs extra capacity, and it can supply the revenues to add such needed capacity.

---

[1] GAO report GAO/RCED-99-234 notes on p. 16 that "For example, because the regulations allow a slot to go unused for up to 20 percent of the time, a carrier with five slots in 1 hour must operate only four flights in that hour on any day to obtain 80-percent use for each of its five slots. The carrier is allowed to "rotate" its four flights across the five slots over the 2-month period to prevent FAA from withdrawing the slot. The practice of a carrier's rotating actual flights among its allocated slots is commonly referred to as 'babysitting.' FAA officials emphasized that babysitting is not prohibited by existing regulation, provided that a slot meets the minimum-use requirements." See http://www.gao.gov/archive/1999/rc99234.pdf

Changing from the traditional, increasingly inefficient administrative controls to a market-based system has generated a fair amount of concern, primarily from the airlines. Change is difficult, and the airlines' concerns are understandable. In fact, very similar arguments were made by the airlines in opposition to deregulation. Concerns were raised about disruption to the industry, lack of a track record, and disruption to business models. However, the ATA Airline Handbook includes a long list of benefits that resulted from deregulation. The Handbook notes that deregulation stimulated competition, led to rapid growth in air travel, and reduced fares by more than 50% in real terms. We believe that market-based remedies directed at congestion will improve airline service like deregulation did.

Why caps must be combined with auctions – and how it will result in lower fares

Implementing caps without any additional market-based mechanism for encouraging competition only increases the cost to consumers, since a lack of competition keeps fares high. A March 2001 Government Accountability Office (GAO) report found that "dominated markets tend to have higher airfares than airports that have more competition from other airlines." Fares in dominated markets averaged 41 percent higher than in markets where there was aviation competition. The difference in fares is largely attributed to the exclusive access granted to incumbent airlines and the incumbent airlines' ability to prevent new entrants from gaining entry to create a competitive market. Instituting slots without a market-based mechanism creates just this exclusivity of access by granting extensive landing rights to incumbent airlines and barring new, competitive entrants into the country's busiest airports.

Granting slots without market-based mechanisms creates a system where incumbent airlines fight to maintain large shares of the airport traffic and to limit the ability of low-cost carriers to compete. The 1996 DOT report *Low Cost Airline Service Revolution* details this anticompetitive culture at capped or dominated airports. The report identifies slot hoarding as one of the key characteristics of such a culture. Federal regulations require airlines to use their slots at least 80% of the time in order to retain possession of them. However, by splitting up larger flights into smaller ones ("downgauging") or by setting up a rotating schedule, airlines have unnecessarily taken up more slots than they would require to competitively serve their customers. Slot hoarding prevents new entrants from taking available slots and increases airplane throughput without increasing passenger throughput, adding greatly to congestion. The report maintains that the high fares charged at these dominated airports create incentives for an airline to use anticompetitive measures to discourage new entrants.

Using the historical backdrop of slots as a guide, we believe that integration of a market-based system into the proposal for slot caps is necessary to protect consumers and a competitive market. Estimates from the DOT's 1996 report valued savings from new entry competition at 35 percent for round-trip flights and 40 percent for one-way flights. A case-specific study on the effect of Southwest Airlines noted that with the opening of just one route between Oakland International Airport and Ontario International Airport in Los Angeles, fares dropped 60% and traffic tripled, increasing both passenger throughput as well as savings for consumers. Even nearby airports not directly offered service experienced a decrease in fare costs of up to one-third. Southwest is just one example of low-cost carriers whose entry into the market drove down prices and increased passenger throughput at previously dominated airports.

What have we proposed?

Last month, the FAA published notice of a proposed rule that would replace the orders imposing operating limits at JFK and Newark and establish a new rule limiting operations at these airports. Instead of reliance on repeated piecemeal approaches to limit and manage operations at JFK and Newark, we believe a better course is to adopt a longer-term rule dealing with the congestion and delays that we expect to persist at those airports. Although we continue to work toward capacity improvements, this proposal will complement capacity enhancement efforts.

Like the proposal for LaGuardia that I discussed the last time I was before this Committee, this proposal recognizes that a simple imposition of caps without some mechanism to ensure preservation of competitive market forces is inadequate. While this proposal is similar to and intended to mesh with the LaGuardia proposal, neither is reliant on the other for final action.

Under the proposal for JFK and Newark, all airlines operating at Newark and JFK would be given up to 20 slots a day for the 10-year life of the rule. The proposal offers two options for JFK. Under the first, 10 percent of the airline's slots above the 20-slot baseline would be made available via an auction. The revenue from those auctions would then be invested in congestion and capacity improvements in the region.

Under the second option for JFK, the airlines would auction 20 percent of slots above the 20-slot baseline and keep all of the proceeds. Depending on the option, between 91 and 179 slots at JFK would be affected out of 1,245 total slots at the airport.

The proposal also calls for auctioning 10 percent of slots at Newark Airport above the baseline annually for the first five years of the rule. As a result, only 96 slots out of a total of 1,219 slots at the airport would be auctioned over the 10-year span of the proposal.

As with any pricing plan pursued by the Department, this proposal for JFK and Newark complies with our international obligations and will not competitively disadvantage domestic carriers. Under this proposal, foreign carriers and domestic carriers are treated the same.

As with the LaGuardia proposal, under this proposal, airlines operating at the two airports would receive a 10-year interest in some of the world's most valuable aviation assets, free of charge, free of question, and free of hassle. Additionally, this proposal – just like the LaGuardia proposal – increases competition by creating a robust secondary market for trading of slots and allowing a way for new entrants to gain entry into a restricted airport.

Conclusion

Mr. Chairman, I appreciate the opportunity to explain to you our proposals for the New York-area airports. We are firmly committed to the idea that any long-term solution to mitigate congestion in the Nation's airspace must include a market-based mechanism. Caps alone have proven to be insufficient, and perpetuating the kinds of delays we experienced in the summer of 2007 is not tolerable.

I would be pleased to provide you or your staff with any additional information that might help explain our proposals and I would be happy to answer any questions you might have.