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I. INTRODUCTIONI. INTRODUCTIONI. INTRODUCTION

Revenues from aviation excise taxes currently fund the majority of the programs of the Federal Aviation Administration (FAA). These tax revenues are deposited into a trust fund that in turn supports most of the FAA's programs. The FAA also receives a portion of its budget from the general tax revenue of the federal government. Opinions vary on whether or not this is the best way for the FAA to be funded.

One goal of the Commission is to recommend the best way for the FAA to raise and spend revenue. This paper will outline some of these options. After discussing some background issues, such as the general budget process and the current aviation taxes, this paper will explain the budget ramifications of several options which would alter aviation revenue collection and spending. Since many aviation industry groups are focusing on replacing all or some of the aviation excise taxes with user fees, a separate paper contains a detailed discussion on non-budgetary issues related to user fees.

Please note that this paper uses the term "user charge" as a general term to encompass user fees, taxes, and charges. There has been much confusion over the use of the terms "user fees" and "taxes" because each one can mean different things to different people. For the purposes of the federal budget, user fee does <u>not</u> have any statutory definition, nor does it refer to a separate budget category for collections of money by the government. User fee is a general term that refers to something charged to users directly availing themselves of, or subject to, a governmental service, program, or activity, in order to recover the government's costs.

How a particular user charge is classified under federal budget rules is the important consideration. In that regard, user charges can be classified as either general revenues or offsetting collections (both of which are explained in more detail below), depending on whether the charge results primarily from the exercise of governmental powers or from business-like activity. In the debate involving aviation user fees and taxes, user fee is usually a reference to some type of offsetting collection. Nevertheless, user charges can be constructed in many ways; how a particular user charge is constructed will determine exactly how it is classified by those who oversee the federal budget process.

This paper does not include a recommendation on what type of system should be adopted for aviation user charges and/or the spending process. This paper is an attempt to define various options and frankly discuss their pros and cons.

II. GENERAL BUDGET INFORMATIONII. GENERAL BUDGET INFORMATIONII. GENERAL BUDGET INFORMATION

The Federal Government operates on a fiscal year that starts October 1. For example, fiscal year 1997 began on October 1, 1996. The FAA's budget process starts when it begins internal deliberations on funding levels, about 18 months prior to the start of the fiscal year. The FAA formulates its budget request and submits it to the Office of the Secretary of Transportation (OST) approximately 15 months prior to the start of the fiscal year. After several rounds of negotiations, OST settles on its budget proposal (which includes funding for the FAA and other modes of transportation) and submits it to the Office of Management and Budget (OMB) 12 to 13 months prior to the start of the fiscal year. OMB must negotiate and develop the President's entire budget based on the requests of every department and agency; this is completed when the President's budget is submitted to Congress 8 months prior to the start of the fiscal year.

The President's Budget is simply a request or proposal to Congress. Although many requests that the President makes are ultimately included in the final budget, Congress passes its own budget proposals. The Congressional budget process begins with a budget resolution. This is an overall Congressional framework on what funds should be raised and how they should be spent. Various assumptions are made as part of the budget resolution (e.g., the aviation taxes are assumed to raise a specific amount during each fiscal year), but Congress does not have to adhere to the specifics of the budget resolution. Most of the specifics are determined through the appropriations process or budget reconciliation (which is legislation used to bring existing revenue and spending law into conformity with policies in a budget resolution).

The budget resolution tells each committee how much money it will need to raise and how much money can be spent. Revenue raising is almost exclusively within the jurisdiction of the tax-writing committees -- the House Ways and Means Committee and the Senate Finance Committee. However, the collection of monies in the form of user fees is primarily within the jurisdiction of authorizing committees, such as the House Transportation and Infrastructure Committee and the Senate Commerce, Science, and Transportation Committee. As discussed in more detail below, federal spending is divided into two budgetary categories: discretionary and mandatory. Most of the discretionary spending assumed in the budget resolution (e.g., defense, national parks, and transportation) will be in the jurisdiction of the appropriations committees. Mandatory spending (e.g., Social Security, Medicare, and food stamps), which accounts for approximately 68 percent of Federal Government spending, is under the jurisdiction of the authorizing committees, usually primarily the House Ways and Means Committee and the Senate Finance Committee. The discretionary spending assumed in the budget resolution is allocated to the committees in a two-step process: first, the spending levels are distributed to the committees (primarily the appropriations committees), and, second, each committee divides the amount allocated to it among its programs or subcommittees.

The Federal Government's discretionary spending is implemented through appropriation bills. There are 13 major appropriation bills; each must eventually pass the House and the Senate in an identical form and be signed by the President. If an appropriations bill is not signed by the President by October 1, those agencies funded by that bill will have to shut down non-critical operations until Congress and the President approve some form of funding for its operations. A reconciliation bill includes changes in Federal Government revenues. A more detailed description of the budget process, including a budget glossary from the President's Budget, is attached.

During the entire Congressional budget process, there are restrictions on spending and revenue raising to control or reduce the federal deficit. The Budget Enforcement Act (BEA) of 1990 divides non-defense Federal Government spending into mandatory spending (also called direct spending) and discretionary spending. **Mandatory spending** (e.g., entitlements such as Social Security old age benefits) requires authorization, not appropriations action. **Discretionary spending** may occur only when funds are appropriated. There are two different budget rules to control these two types of spending: mandatory spending is controlled by "pay as you go" rules, and discretionary spending is controlled by spending caps.

Mandatory spending is usually included in bills authorizing various federal programs. Once in place, a mandatory program receives annual funding sufficient to provide the benefits specified in law without any additional Congressional action. Laws providing mandatory spending often do not include expiration dates. Therefore, to stop, lower, or increase the funding level of a mandatory program, Congress must pass, and the President must sign, another bill. This is in contrast to discretionary spending, which is usually limited to one year. As already mentioned, to control mandatory spending, Congress must abide by the "pay as you go" (or PAYGO) rules. In its simplest form, PAYGO means that any new mandatory spending must be offset by changes in mandatory revenues (i.e., virtually all taxes) or mandatory spending. For instance, if Congress decided that the FAA should become a mandatory program, Congress would have to implement mandatory revenues (taxes), or cuts in mandatory spending (not discretionary), that are equal to the proposed mandatory spending. However, the FAA is actually a discretionary program, so a bill that included a reduction in aviation taxes could not offer a reduction in FAA spending as a PAYGO offset because the taxes are mandatory and the FAA's spending is classified as discretionary. If a bill including new mandatory spending is considered for passage and there is no PAYGO offset (i.e., mandatory revenue increase or mandatory spending decrease), the bill can be struck down in the House or Senate by a parliamentary point of order because it would increase the federal deficit; however, budget points of order can be waived in the Senate, usually by a three-fifths majority vote, and in the House by a protective Rule or unanimous consent.

Discretionary spending is controlled with budget caps. As discussed above, the budget resolution develops overall spending levels which are allocated to each committee (with virtually all discretionary spending allocated to the appropriations committees). Each appropriations committee then decides how much each of its subcommittees will be allowed to spend for a fiscal year.

The FAA belongs to a group of agencies that for budgetary purposes is called Function 400. Function 400 includes the FAA, most other DOT agencies and programs, the National Transportation Safety Board, and a few other small agencies. A spending limitation is decided each year for Function 400. Within that spending limitation, the appropriation committees (through their subcommittees) must decide what funding level each agency will receive.

Therefore, if the FAA needs a 12-percent raise to pay for its operations, other transportation modes (e.g., Coast Guard, highways, and transit) may have to suffer reductions. Likewise, if other modes of transportation need additional funding, the FAA's funding level might be reduced to a point that would not support all of the FAA's current needs.

The FAA's budget is divided into four accounts: (1) **Operations**, which supports FAA air traffic controllers, aircraft and airline inspectors, security specialists, and headquarters staff; (2) **Facilities and Equipment** (F&E), which supports capital equipment expenses such as new radar, air traffic control towers, and the new air traffic controller equipment; (3) **Airport Improvement Program** (AIP) Grants, which supports capital needs at airports such as new runways and taxiways; and (4) **Research, Engineering, and Development** (RE&D), which supports various research projects including developing improved explosive detection equipment and lighter and stronger material for aircraft manufacturing.

The table below shows the FAA's funding levels for the past four years and the President's 1998 request. The FAA's funding has increased and decreased, but overall the funding level has been between $8 billion and $8.5 billion. On an account-by-account basis, Operations received the largest increase in fiscal year 1997 over fiscal year 1996 ($312 million or a 7 percent increase). The FAA's overall increase was only 5 percent; thus, a proportionately higher amount was given to the Operations account in 1997. As the table also indicates, there has been a fairly steady decline in FAA investments over this period. A more detailed discussion of the FAA's financial requirements will be presented in the Financial Requirements paper for the Commission.

FAA APPROPRIATIONS 1994-1997
(dollars in millions)

Account	1994	1995	1996	1997	1998 President's Request
Operations	4,579.0	4,572.1	4,642.7	4,954.9	5,386.1
Facilities and Equipment	2,054.7	1,960.4	1,855.1	1,937.5	1,875.0
Airport Grants	1,690.0	1,450.0	1,450.0	1,460.0	1,000.0
Research	254.0	251.6	185.7	208.0	200
Total	8,577.7	8,234.1	8,133.5	8,560.4	8,461.1

III. CURRENT AVIATION TAXES, THE AVIATION TRUST FUND, AND THE GENERAL FUND CONTRIBUTIONIII. CURRENT AVIATION TAXES, THE AVIATION TRUST FUND, AND THE GENERAL FUND CONTRIBUTIONIII. CURRENT AVIATION TAXES, THE AVIATION TRUST FUND, AND THE GENERAL FUND CONTRIBUTION

In fiscal year 1998, the aviation taxes that go into the Airport and Airway Trust Fund (Trust Fund) have the potential of raising approximately $7 billion. However, the aviation taxes have raised less than this amount over the past few years because the taxes were allowed to expire in fiscal years 1996 and 1997 (see table below). There are three excise taxes imposed on commercial air transportation: (1) 10 percent tax on the price of domestic air passenger tickets; (2) $6 per passenger international departure fee; and (3) 6.25 percent tax on domestic air freight. General aviation is subject to taxes on fuel: 17.5 cents per gallon for jet fuel and 15 cents per gallon for aviation gasoline. Historically, about 87 percent of the excise tax revenues come from the tax on domestic airline tickets.

All of these taxes are deposited into the Trust Fund, which was established in 1970 to finance a portion of the FAA's costs. Before the establishment of the Trust Fund, the functions of the FAA were supported by General Fund revenues. Aviation system users also pay other taxes, such as the 4.3 cents-per-gallon fuel tax for deficit reduction (surface transportation modes are also charged this fee), airline corporate income tax, and a variety of customs and agriculture charges. However, these taxes and charges are not deposited into the Trust Fund.

Aviation Tax Revenues 1994-1997
(dollars in millions)

	1994	1995	1996*	1997* (estimate)	1998 (estimate)
Passenger Ticket Tax	4,528.2	4,767.6	2,122.9	4,191.0	6,057.1
Waybill	283.9	361.3	150.9	324.0	425.6
General Aviation Fuel Tax	159.1	171.9	(33.2)	137.0	154.0
$6 International Departure Fee	218.1	233.0	128.4	224.0	302.7
Total	5,189.3	5,533.8	2,368.9	4,876.0	6,939.4

*Tax revenues were lower in 1996 and 1997 because the aviation taxes expired and were not reinstated immediately.

Through the 1980s, the uncommitted balance (a/k/a surplus) in the Trust Fund grew from approximately $2 billion to approximately $7 billion. In spite of the existence of the Trust Fund, the programs funded by the Trust Fund were subjected to federal budgetary pressures to limit the growth in spending while the revenue from the excise taxes grew automatically due to increased aviation system usage. The large Trust Fund balance reduced the overall federal deficit. Whether purposeful or not, much of the aviation community believes that spending is being restrained and taxes maintained so that the federal deficit appears smaller. The large uncommitted balances indicated that the Trust Fund was “broken.”

The aviation taxes, which periodically approach an expiration date but are typically reauthorized before they expire, actually did lapse at the end of 1995. This was in the midst of the budget showdown between the President and the Congress. While there were insurmountable differences at that time between the President and the Congress on how to balance the budget, one aspect of all budget plans at the end of 1995 was a continuation of the aviation excise taxes. When budget negotiations halted in early 1996, the taxes had lapsed and there was no effort to reinstitute them on a stand alone basis until late in the year, and then they were only reauthorized for the last four months of 1996. This caused the Trust Fund’s uncommitted balance to drop from $5 billion in fiscal year 1995 to $2.4 billion in fiscal year 1996.

The taxes again lapsed at the end of 1996, and again the Trust Fund balance began a precipitous decline since there were no replenishing revenues. In February, it was discovered that most of the anticipated revenues from the Fall of 1996 had actually not been remitted by most of the airlines through a legal deferral. This deferral had not been assumed in Trust Fund balance calculations, and when this was learned it became readily apparent that the portion of the FAA funded by the Trust Fund would not have a source of funding in a matter of weeks. In the face of this, Congress passed legislation extending the taxes through the end of the current fiscal year (September 30). It is estimated that the balance at the end of fiscal year 1997 will be $2.5 billion.

For fiscal year 1997, the Trust Fund will support 62 percent of the FAA’s budget. General Fund revenues (i.e., general taxes) will support the remaining 38 percent. Although the Trust Fund was created primarily to support the FAA’s capital investments, the FAA’s Operations account has, over the years, received an increasing level of Trust Fund support. The amount of Trust Fund monies available to support FAA Operations is determined by the lower of two statutorily-defined calculations: (1) 50 percent of the appropriations for the FAA's capital accounts (F&E, RE&D, and AIP); or (2) 72.5 percent of the FAA's entire budget minus the amount of the FAA's appropriations for all the capital accounts. General Fund revenues support the remainder of the Operations account budget.

Some people believe that the FAA should be 100 percent supported by the Trust Fund. Aviation users would have to pay approximately $2 billion more each year to fully support the FAA’s existing level of expenses. Other people believe that FAA services provide benefits to all U.S. taxpayers and therefore should be partially supported with General Fund revenues.

During a recent hearing before the Subcommittee on Aviation of the House Committee on Transportation and Infrastructure, several witnesses testified that the FAA should be partially funded by general tax revenues because aviation system benefits our society as a whole, not just system users. The general consensus was that non-aviation users benefit economically and socially from a safe, efficient, and effective air transportation system. Examples of this benefit included the following: increased property values and employment levels in areas which have adequate access to air transportation; people who benefit from the air transportation system without getting on a plane include cab drivers, hotel employees, and shop workers who manufacture goods destined for the global economy; and all members of our society benefit from a safe aviation system that prevents fatal aircraft accidents. One witness mentioned a study by Wilbur Smith Associates which estimated that "the U.S. air transportation system generated $771 billion in economic activity -- 5.9 percent of our nation's GNP in 1993." From this figure, the witness estimated that ". . . civil aviation contributes directly, indirectly or through induced impacts, roughly $30 billion in federal taxes each year, an excellent return on the government's $2 billion annual investment."

While acknowledging the general benefits that the aviation system provides to non-system users, some would dispute the logic of requiring a General Fund contribution be made to the FAA in recognition of those benefits. These observers point out that the interstate freeway system also provides many general societal benefits, and yet it is entirely user funded. If the users entirely fund the aviation system, the costs of that system are ultimately distributed to the broader society as a component of such things as the price of shipping a package by air. Requiring the Federal Government to support part of the system means that the money supposedly representing the general benefit to society will flow inefficiently through a bureaucratic and political system rather than the marketplace.

In addition to the general benefit to society, there are other government users of the aviation system that are not charged aviation taxes, specifically the U.S. military and other government aircraft. Military aircraft use the FAA air traffic control system every day. Some aviation users argue that the General Fund contribution reflects the amount the U.S. military and other government agencies use FAA's air traffic control system and, therefore, should continue. This issue is discussed in greater detail in the paper on Cost Allocation.

Nonetheless, some aviation analysts believe that FAA should be supported 100 percent by user charges. One advantage of eliminating the General Fund contribution is that FAA could be largely removed from the federal budget process if it is largely supported by cost-based user fees. If the FAA is supported with a combination of user fees and General Fund revenues, a portion of the FAA's budget would still be subjected to budget caps and possible budget cuts. An FAA that is 100 percent user supported could be legislatively constructed so that the user charges are collected and spent considering only the FAA's needs and revenues. Nevertheless, it may be difficult to convince some civil aviation users to pay 100 percent of FAA's costs while the military uses the system without somehow paying for its share of the costs. Regardless of the intellectual merits of this discussion, the continuing pressure on reducing the federal deficit is very likely to mean a decrease in the General Fund contribution, or an increase in the Trust Fund balance.

IV. THE BUDGET RULES AND FAA’S REVENUES AND SPENDINGIV. THE BUDGET RULES AND FAA’S REVENUES AND SPENDINGIV. THE BUDGET RULES AND FAA’S REVENUES AND SPENDING

The Congressional Budget Office (CBO) predicts a $67 billion federal deficit (borrowing that takes place over one fiscal year) by the end of fiscal year 1997. In 1997, the federal debt (the accumulated total of previous federal borrowing) is expected to be $3.8 trillion, and the net interest on the debt will cost taxpayers $248 billion. The public’s general consensus is that these deficit figures need to be reduced or eliminated. Tight controls have been placed on federal spending and revenues in an attempt to minimize these deficit figures.

As mentioned above, federal revenues and spending, including that of the FAA, are controlled in part by the Budget Enforcement Act (BEA). In its simplest form, the BEA requires that changes in taxes or spending cannot increase the expected federal deficit. What many members of the aviation industry want are fair aviation user charges that are used to support FAA programs. The question is, will these proposals to change the user charges and/or allow the FAA to spend more money comply with BEA requirements? And if not, can those requirements be changed?

There are two budget rules or assumptions that significantly affect FAA revenues and spending: (1) the assumption that aviation excise taxes are permanent, even if statutorily they are scheduled to expire; and (2) the classification of FAA spending as discretionary spending subject to annual budget caps while the revenue is mandatory.

(1) Aviation Taxes are Assumed to be Permanent: Historically, aviation taxes have been assumed to be a permanent revenue stream. Therefore, when the budget resolution is negotiated each spring or summer, Congress depends on a certain amount in annual aviation tax revenues. This creates a problem if a member proposes to change the taxes. Taxes are considered mandatory revenue, while user fees are usually considered discretionary revenue (e.g., offsetting collections). Therefore, under normal circumstances, if Congress wanted to adopt aviation user fees in place of aviation taxes, the BEA would require an offset of mandatory spending or mandatory revenues (PAYGO offset) because the mandatory aviation taxes would be eliminated.

Recently, the aviation taxes expired. Because they did not appear in the “snapshot” of the federal budget taken by CBO each January for its baseline calculations, the taxes were no longer considered permanent. This situation created an unusual budget rule loop-hole -- any reinstatement of the aviation taxes would be considered new revenue for budget resolution and reconciliation purposes. That means that if Congress wanted to establish an aviation user fee instead of reinstating the existing taxes, a PAYGO offset would not be needed (because the aviation taxes were not assumed to be in existence). That also means that any new aviation user tax (including reinstating the 10 percent ticket tax) would provide an offset for new mandatory spending or mandatory revenue cuts. For example, reinstating the aviation taxes could be used as a PAYGO offset to a middle-class tax cut or to an increase in Medicare benefits. This budget rule loop-hole transformed passing the aviation taxes from an uneventful reinstatement process to a potential fight over which programs will benefit from the aviation taxes' PAYGO offset.

Although not all of the information about the recent budget agreement is public, the Commission staff have been informed that the budget resolution assumes that there will be revenue equivalent to reinstating the aviation taxes for 5 years. Therefore, any proposal to adopt a true user fee system would require a PAYGO offset. Because true user fees are usually considered discretionary revenue, either an increase in taxes or a decrease in mandatory spending would be necessary to pass a true user fee proposal with a simple majority in each house of Congress. As mentioned above, the PAYGO restrictions can essentially be waived with 60 votes in the Senate, and with unanimous consent or a special Rule in the House.

(2) The Classification of Trust Fund Spending as Discretionary Spending subject to Annual Budget Caps while the Aviation Revenue is Mandatory: Even though the FAA has a Trust Fund that is fully supported with revenues from aviation users, the FAA is funded through the appropriations process and must compete with other modes of transportation. The budget cap that is placed on the Department of Transportation and related agencies does not take into consideration that the FAA has a seemingly dedicated revenue stream derived from its users. Although the FAA's spending is considered discretionary, the revenue supporting the Trust Fund is considered mandatory. Therefore, **there is very little relationship between the revenues flowing into the Trust Fund and the level of the FAA funding**. For instance, in 1995, there was a $5 billion uncommitted balance in the Trust Fund; however, the FAA's appropriations were reduced 4 percent from the 1994 level. On the other hand, at the beginning of fiscal year 1997, the aviation taxes had not been extended through the entire fiscal year and there was a question as to whether the Trust Fund balance could support the FAA. Regardless of this uncertainty, the FAA was appropriated $8.6 billion for 1997, a 5 percent increase from 1996.

This budget classification also means that if the FAA proposes a program that would significantly reduce its costs, there would not be a corresponding reduction in aviation taxes. Since the FAA's spending is discretionary, any cost savings could only benefit other discretionary programs.

V. BUDGET REVENUE CATEGORIESV. BUDGET REVENUE CATEGORIESV. BUDGET REVENUE CATEGORIES

Before exploring different types of aviation user charges, the Federal Government's revenue categories should be discussed. Money collected by the Federal Government is classified into two major categories: general revenues and offsetting collections.

A. General RevenuesA. General RevenuesA. General Revenues

Definition and examples: General revenues (also called governmental receipts) are taxes and other collections from the public that result from the exercise of the Government's sovereign or governmental powers, such as individual and corporate income taxes, social security taxes, excise taxes, estate and gift taxes, and customs duties. In the aviation realm, these receipts include the taxes on domestic air passenger tickets, international departure tickets, domestic air cargo and non-commercial aviation fuels, as well as corporate income taxes. Unlike offsetting collections, general revenues can only be spent for FAA programs when specific appropriation bills are passed.

Role of the Executive Branch and Congress: The Administration may propose changes to tax law, but tax bills must be initiated in the House. The House Ways and Means Committee and the Senate Finance Committee have jurisdiction over tax laws.

Budget treatment: General revenues are scored as mandatory. If a new law proposes to decrease general revenues, the impact must be accounted for on a PAYGO basis. As required by the BEA, OMB estimates the net effect on the deficit of enacted laws that affect mandatory spending and receipts. If there is an estimated net increase in the deficit for the current fiscal year as a result of new legislation, the BEA specifies sequester procedures for the uniform reduction of most non-exempt mandatory spending programs. Only 3 percent of all mandatory spending is sequesterable by either uniform reduction or special rule; the rest is exempt from sequester by law.

In estimating the amount of excise taxes that will be collected, the government typically makes a downward adjustment (for the total of the mandatory accounts) of 25 percent to reflect the impact these tax collections have on total federal tax collections (in part because the excise taxes would be tax-deductible business expenses).

Pros:

- They may be authorized for a number of years, leading to more continuity and less guesswork about future financing.
- They do not need to be based on highly accurate cost allocation.

Cons:

- To some, they are distasteful because they either are, or resemble taxes.
- Some may dislike them because they are not necessarily based on accurate cost allocation.
- Taxes raised from a specific industry will not necessarily be spent to support industry priorities.

B. Offsetting CollectionsB. Offsetting CollectionsB. Offsetting Collections

Definition and examples: Offsetting collections are income the Federal Government earns from its various business-type activities, such as the sale of postage stamps and electricity, admittance fees to national parks, premiums for deposit insurance, and proceeds from the sale of government-owned land. Offsetting collections may also be monies flowing from one Federal entity to another for goods or services provided. Agencies usually are able to collect and spend offsetting collections established in law in addition to their appropriations levels.

Role of the Executive Branch and Congress: The Administration may propose to Congress that offsetting collections be authorized. Any proposal by FAA/DOT would need to be approved by the OMB. Congress may go along with the Administration's proposal or come up with its own version.

Offsetting collections may be classified as mandatory or discretionary; very basically, they are mandatory if created in authorization law and discretionary if created in appropriations law.

Budget treatment: Offsetting collections from the public are deducted from gross budget authority and outlays, rather than combined with general revenues. In other words, they make room for themselves in the federal budget. With certain exceptions, agencies are usually allowed to spend what they estimate they will raise as offsetting collections. For instance, in 1997, funding for FAA's F&E account is $1.938 billion in direct appropriations plus $100 million in offsetting collections, totaling $2.038 billion in gross budget authority made available to the F&E account.

Pros:

- They are applied to those people or entities who benefit from goods or services provided.
- In an era when taxes are a political issue, these collections are not taxes.
- They have the potential to raise needed funds that are becoming increasingly unavailable in the Federal Government's overall budget.
- Funds raised are easily spent, without a lengthy Congressional approval process.
- Mandatory offsetting collections may be established for multiple years.
- Discretionary offsetting collections may be used for discretionary spending, like that of the FAA.

Cons:

- Discretionary offsetting collections established by appropriations are only good for one fiscal year at a time.
- Offsetting collections (such as fees) may be opposed by the tax-writing committees of Congress, who would prefer revenues to be taxes and, therefore, within their jurisdiction.
- The tax committees may interpret a fee as a tax, unless a strong case can be made that the charges are accurately directed at a class of beneficiaries and directly related to the services provided, and are not used for other purposes.

VI. BUDGET TREATMENT OF VARIOUS REVENUE AND SPENDING PROPOSALSVI. BUDGET TREATMENT OF VARIOUS REVENUE AND SPENDING PROPOSALSVI. BUDGET TREATMENT OF VARIOUS REVENUE AND SPENDING PROPOSALS

The following are brief explanations of various ways in which the FAA's revenue and spending could be altered and the resulting budget implications. This information should be considered an introduction to these issues. Each type of user charge or revenue stream can be easily complicated by budget rules and the legislative language that creates it. The proposals are discussed in the following order:

A. Status Quo
B. Changing the FAA's Revenue Source
C. Changing the FAA's Spending
D. Changing Both the FAA's Revenues and Spending
E. Other Innovative Financing Options

These proposals are not necessarily mutually exclusive. One proposal that gives the FAA more funding could be paired with a proposal that changes the aviation user charges. The descriptions below discuss examples that closely relate to FAA's circumstances. However, there may be other situations where the same user charge or revenue stream is treated slightly differently under the budget rules. If we discover additional information regarding user charges and revenue streams, it will be provided to the Commissioners.

A. Status QuoA. Status QuoA. Status Quo

<u>Definition, Role of Congress, and Role of the Executive Branch</u>: The FAA's taxes remain the same and the FAA's budget is authorized and appropriated by Congress. The Executive Branch implements the FAA's budget according to Congressional specifications.

<u>Budget Treatment</u>: The aviation taxes are mandatory revenue and, therefore, may not be reduced without a PAYGO offset. The FAA's spending is discretionary and, therefore, is limited by the discretionary budget caps.

<u>Pros</u>:

- Some members of the aviation industry believe the taxes are fair and should not be changed.
- The current taxes are relatively easy to collect.
- Congress has significant control over FAA spending which provides checks and balances on the FAA.

<u>Cons</u>:

- Some members of the aviation industry do not believe the taxes are fair.
- Because the taxes are mandatory revenue and the spending discretionary, there is no relationship between the level of aviation user charges collected and the level of FAA's budget.
- Long-term investment decisions are very difficult to make when subjected to the annual budget and appropriations process.
- As overall federal discretionary spending is reduced or tightened, needed funds probably will not be available.

B. Changing the FAA's Revenue SourceB. Changing the FAA's Revenue SourceB. Changing the FAA's Revenue Source

1. Adopt New Taxes. Adopt New Taxes. Adopt New Taxes

Definition and Example: The current aviation taxes could be replaced with a different type of aviation tax. For instance, the 10 percent ticket tax could be replaced with a fuel tax or a tax based on the weight or capacity of an aircraft.

Role of Congress: Any new taxes would have to be implemented by Congress. Such a bill would have to be initiated in the House Ways and Means Committee. The Finance Committee would have jurisdiction over the bill in the Senate. The authorizing and appropriations committees in both houses would request to participate in the development of a new tax. Congress would still appropriate the FAA's budget.

Role of the Executive Branch: There would be no real change in the current role of the Executive Branch.

Budget Treatment: The new taxes would have to equal or exceed the revenue generated by the current taxes, otherwise a PAYGO offset would be needed (i.e., an increase in mandatory revenues or a reduction in mandatory spending equal to the revenue shortfall). The FAA's budget would continue to be authorized and appropriated by Congress. There would be no expected increase in the FAA's budget level.

Pros:

- The new taxes could be structured to better reflect the costs users impose on the system.

Cons:

- In addition to the disadvantages of the Status Quo mentioned above, the FAA's budget would continue to be constrained by discretionary budget caps.
- The aviation user charges would not truly reflect the costs users impose on the system.

2. Aviation Infrastructure Bank. Aviation Infrastructure Bank. Aviation Infrastructure Bank

Definition and Example: In 1995, the two principal airport trade associations (ACI-NA and AAAE) proposed the creation of the National Aviation Infrastructure Development Bank (NAIDB). Although loosely described as a "bank," it would not strictly follow traditional banking and deposit and lending practices.

Under the ACI/AAAE proposal, the funding mechanism would be managed by a not-for-profit organization, NAIDB, established by Congress. The NAIDB would be empowered to issue debt and provide funding for the FAA Facilities and Equipment (F&E) budget, the AIP budget, the Contract Tower program, and the Essential Air Service program. (It should be noted that since the NAIDB proposal was put forth, the EAS program has met its funding needs (up to $50 million per year) through another mechanism.) The NAIDB also would be empowered to collect user fees equivalent to 40 percent of the existing aviation excise taxes. The remaining federal aviation excise taxes would be reduced by a corresponding amount, and, along with General Fund contributions, would continue to fund FAA operations. According to proponents, the NAIDB could be structured to result in a reduced General Fund contribution.

The NAIDB would be authorized to provide funding of grants to airports for projects currently eligible under AIP standards. Individual grants would be subject to approval by the FAA. This entity also would provide funding to the FAA for the capital portion of the F&E program, as authorized by Congress. The F&E funding could be a mixture of direct funding from user fee collections in any given year and bond proceeds from tax-exempt debt issued by the NAIDB and serviced by user fee collections. The NAIDB also would be authorized to provide funds for the portion of the Contract Tower Program that would become ineligible under cost-benefit criteria issued by the FAA in September 1995. Finally, it could issue guarantees and credit enhancements for debt issues of less than $15 million by small and non-hub airports and for other innovative airport financing arrangements.

As proposed in draft legislation, the NAIDB would not be a government entity, its revenues and expenditures would not be part of the federal budget, its user fees would not be taxes, and its debt would be private, not backed by the federal government. The draft legislation grants one-time authority to collect user fees. The user fees would be collected in the same manner as the present aviation excise taxes under new regulations to be issued by the FAA. The NAIDB would be governed by a board of trustees.

Role of Congress: Besides enacting the underlying legislation, Congress would continue to impose the existing user taxes at a reduced rate and appropriate those revenues for the Operations portion of the FAA budget. For the most part, the role of Congress and its relevant committees would remain the same.

Role of Executive Branch: The role of the Executive branch would remain unchanged except for the monies handled by the NAIDB. Although the original proposal is not entirely clear, the NAIDB would provide the FAA with funds for capital investments at the direction of the FAA.

Budget Treatment: The NAIDB and similar proposals encounter numerous budgetary and legal difficulties. The government's ability to give a non-governmental entity the power to tax (or even charge fees) is a very significant issue. The key question is whether the new entity is going to be carrying out a governmental function. If so, it would be a governmental entity and its spending would be subject to federal budget constraints. If not, it might be a government sponsored enterprise (GSE) similar to Fannie Mae and not have its spending be any part of the federal budget. In this case, the Congressional Budget Office (CBO) most likely would consider the NAIDB, as originally proposed, to be a federal entity for budget scoring purposes since it would be "taxing" users to pay for airport grants and other infrastructure costs. If the NAIDB spent more money than it brought it in a particular fiscal year, there would be a PAYGO spending problem.

Issuing debt is the same thing as spending under budget scoring rules. Because issuing debt involves spending more in the early years than it is bringing in through fees (even if it would mean bringing in more in later years), there would be a PAYGO problem and some type of waiver or offset would be required. In addition, according to a CBO analyst, there would be scoring problems with other activities of the NAIDB. For example, loan guarantees are treated as cash outlays in the amount of the net present value of the risk of default. The tax-exempt bonds are also reportedly problematic.

On a separate note, because user fees should only be charged for voluntary, business-type services, they arguably cannot be charged to finance grants for airports and other infrastructure needs. Supporters of the NAIDB concept assert that infrastructure projects constitute the provision of service.

Pros:

- If the original NAIDB proposal can be reconstructed to become like a GSE, rather than a government entity, it would be outside of budget constraints and have many advantages and be one way to ensure that monies raised from users are spent for intended purposes. It could leverage a revenue stream for infrastructure development and be able to provide for long-term capital investments in a business-like manner.
- One of the main obstacles to the concept as originally proposed is the charging of user fees or taxes, which probably would make it a governmental entity. One way around this problem would be having the airports and airlines working together (e.g., through some type of contractual arrangement) to voluntarily contribute to the NAIDB. (PFC revenue might be a component of such an arrangement.) Under such circumstances, the NAIDB probably would not be a governmental entity. Of course, adjustments would still have to be made to the tax rates and discretionary spending caps to reflect what would, in essence, be the off-loading of capital expenditures from the budget. Because the tax-writing committees are reportedly counting on that revenue this year for use in offsetting

tax cuts, it would be difficult to eliminate 40 percent of the revenue from aviation excise taxes while converting it to user fees.

Cons:

- The budget treatment concerns are the most obvious issue working against the concept as proposed in draft legislation. If it is deemed to be a governmental entity, there really would not be any benefits to using this structure.

3. Borrowing Authority. Borrowing Authority. Borrowing Authority

Borrowing authority is a possible way to address shortfalls in funding and would allow users to pay for improvements as they benefit from them rather than well in advance, as is done under the current appropriations process. However, because the spending of borrowed funds is treated the same for budgetary purposes as the spending of appropriated funds, there is little advantage to doing so. The Administration's proposal to create a government corporation to run the ATC system, gave that corporate entity the power to borrow funds and issue debt outside of the normal budgetary constraints. An exemption from such budgetary constraints would make this option attractive; however, there would likely be Congressional opposition if the exemptions were perceived as a way to circumvent a balanced budget agreement.

C. Changing the Way the FAA Can Spend Its RevenuesC. Changing the Way the FAA Can Spend Its RevenuesC. Changing the Way the FAA Can Spend Its Revenues

1. Taking the Aviation Trust Fund Off-Budget. Taking the Aviation Trust Fund Off-Budget. Taking the Aviation Trust Fund Off-Budget

Definition and Example: The current aviation taxes should raise approximately $7 billion per year. In 1997, only $5.3 billion will be used from the Trust Fund to support the FAA's programs (an additional $3.2 billion supports FAA Operations form the General Fund). If the FAA's spending remains flat and the current level of taxes remain constant, the uncommitted balance in the Trust Fund could reach over $11 billion in 2002. The balance in the Trust Fund cannot be spent on non-aviation programs, but the balance does make the federal deficit look smaller. In the simplest form, the federal deficit is calculated by adding up total federal revenues and subtracting total federal spending. When the Trust Fund takes in more than it spends, the federal deficit appears smaller.

During the 104th Congress, the House passed a bill which would have taken the transportation trust funds off-budget. The 104th Congress concluded without the Senate taking action. The off-budget bill has been introduced again in the House (H.R. 4). The language in H.R. 4 tracks the language used to take the Social Security Trust Funds off-budget. Specifically, the bill removes the transportation trust funds from: (1) calculations of the on-budget deficit; (2)

congressional budget resolutions, including spending allocations provided to committees, and (3) spending points of order under the Budget Act. The bill also provides safeguards for the Trust Fund (which already exists for the Highways Trust Fund) to ensure that spending out of the Trust Fund does not exceed the balance in the Trust Fund.

The bill essentially allows the FAA to be supported by the Trust Fund without consideration of the spending caps or the federal deficit. If H.R. 4 was implemented, the FAA's budget would be based on the FAA's needs and the balance in the Trust Fund. H.R. 4 would only apply to that part of the FAA budget that is supported by the Trust Fund (the capital accounts and part of the Operations account). The part of the FAA's Operations account funded with General Fund revenues would continue to be subject to budget constraints, such as the discretionary caps and sequestration.

Role of Congress: If H.R. 4 is implemented, Congress' role would not significantly change. H.R. 4 does not change the aviation taxes; thus, the role of the House Ways and Means Committee and the Senate Finance Committees would remain unchanged. The FAA would still have to have authorization and appropriations prior to spending funds. The advantage to the FAA is that the authorization and appropriation levels could be based on the FAA's needs and Trust Fund revenues. Only a portion of FAA Operations (that part supported with General Fund revenues) would continue to be constrained due to budgetary caps on discretionary spending. Only the General Fund supported part of the Operations account would be part of the budget resolution process.

Role of Executive Branch: The FAA, DOT, and OMB would continue to go through their usual budget process.

Budget Treatment: H.R. 4 would exempt the Trust Fund spending from the discretionary spending caps, PAYGO procedures, and Congressional budget controls (including the budget resolution and reconciliation instructions). According to the Congressional Budget Office, taking the Trust Fund off-budget would not, in and of itself, change total spending of the Federal Government and does not require any PAYGO offset. However, H.R. 4 would allow Congressional action that could lead to more funding for the FAA. The portion of the FAA's Operations Account that would be funded with General Fund revenues would still be under the discretionary spending cap and subject to reductions to control the federal deficit. H.R. 4 makes no changes to the aviation taxes

Pros:

- FAA's needs are increasing and the revenues in the Trust Fund are projected to increase (the current taxes will be raising $8.9 billion annually in 2002).
- Taking the Trust Fund off-budget allows this additional revenue to be spent on valid FAA needs.
- Supporters of the off-budget proposal believe that the bill would fulfill a promise made by Congress when it levied user charges on transportation and dedicated these charges to

transportation purposes -- to use the proceeds for their intended purposes and not to mask the size of the deficit.

Cons:

- The General Fund contribution to the FAA's budget would still be vulnerable to cuts due to discretionary budget caps.
- Some people think that the General Fund contribution might be reduced enough that aviation taxes would have to be raised to make-up the difference.
- Taking the Trust Fund out of the unified budget limits the ability of Congress to adjust national spending priorities in the constrained environment of a balanced budget.
- Opponents argue that it is simply a way to increase government spending for projects that put money into virtually every state and congressional district.
- The White House has indicated strong opposition to the proposal, and there is yet to be a sponsor in the Senate this Congress.

2. Revenue Constrained Fund (S. 404). **Revenue Constrained Fund (S. 404). Revenue Constrained Fund (S. 404)**

Definition and Example: S. 404 was introduced in the Senate on March 5, 1997 and specifically addresses changes to the Highway Trust Fund (which impacts the Federal Highway Administration and other surface modes). Since the introduced bill does not include the aviation programs, the discussion below assumes a bill that would be similar to S. 404, but would include the FAA's programs and Trust Fund.

The bill would establish a revenue constrained fund (RCF) which would be exempt from the discretionary caps and PAYGO procedures. Instead, spending for programs would be limited by the previous year's receipts accruing to the fund. This proposal would make all the receipts in the Trust Fund available for obligation without appropriations action. For example, if legislation is enacted by the end of fiscal year 1997 to establish an RCF for the FAA, this year's aviation tax receipts would be available for obligation in fiscal year 1998. The bill also provides for a reduction in the discretionary caps.

Role of Congress: After passing the bill, Congress would no longer need to appropriate Trust Fund monies. Trust Fund spending would be equal to the aviation tax or user fee receipts. The authorizing committees would still need to authorize the FAA's programs. Depending on the legislation and Congressional action, the authorizing committees could adopt a role similar to today's appropriations committees by setting more specific and detailed spending levels in authorization legislation.

The portion of the FAA's Operations budget that receives General Fund revenues would still be part of the budget process and subject to the budget caps. This could mean that the Operations account is funded at lower levels than requested because of the constraints on discretionary spending.

Role of the Executive Branch: OMB would be responsible for determining a final estimate of aviation account revenues collected the previous year. If the actual revenues are lower than OMB's estimate, then the FAA's spending would be reduced to avoid any deficit spending. Although not specified in the bill, the FAA would probably still maintain a budget process to identify spending priorities.

Budget Treatment: The FAA's Trust Fund expenditures would simply be based on revenues and not subject to appropriations or budget caps. The FAA's General Fund expenditures (a portion of the Operations Account) would still need to be appropriated and would be subject to budget controls. Since the bill would allow direct spending, the bill would need a PAYGO offset or waiver. Although the bill requires that discretionary caps be reduced, that is not a true PAYGO offset since the direct spending would be scored as mandatory spending and the reduction in the budget caps are part of the discretionary budget.

Pros:

- Implementing a bill similar to S.404 for aviation would allow the aviation tax revenues to be spent without appropriation actions and without budget caps.
- The only limit to the FAA's spending would be the revenues in the Trust Fund. However, the authorizing committees could choose to limit the authorization levels of the FAA.

Cons:

- It appears that a bill similar to S.404 would require a PAYGO offset or waiver. Finding a mandatory program to cut or additional mandatory revenues to raise could be difficult.
- Cutting the appropriation committees out of the process would make it a difficult bill to pass through Congress due to the anticipated strong opposition from their members.
- There may be a desire to have the FAA justify its budget to Congress to better ensure that the funds are spent in the most effective and efficient manner.

3. Revolving Fund. Revolving Fund. Revolving Fund

Revolving funds have been acceptable mechanisms to support certain operations of the federal government. They typically finance cycles of operations in which the activity is clearly commercial in nature, outlays generate receipts, and collections are earmarked for use in a continuing business-type operation. Given the nature of a revolving fund, it typically would be funded through a user fee (offsetting collection) of some type, such as for ATC services. Receipts from such fees would be deposited into a revolving fund, from which operating and capital expenditures for delivery of services would be made. Once established, such a revolving fund could be self-sustaining, requiring no further Congressional action. A revolving fund essentially involves a form of direct spending.

Establishing a revolving fund for the FAA would require a technical adjustment of the Budget Enforcement Act to lower the discretionary cap by the amount of spending being moved from the discretionary side of the budget to the mandatory side. Thereafter, any revenue increases would permit spending increases. Although the FAA would be provided with considerable flexibility under such a funding arrangement, removing the ATC system from the annual appropriations process would be difficult politically. Appropriators and others in Congress would be reluctant to allow the FAA to have unfettered spending authority without the discipline of the market (since the ATC system is a monopoly) or the appropriations process to reign in costs. However, because a revolving would likely involve a user fee, it would be expected that industry involvement would increase and provide oversight and discipline similar to the appropriations process. Furthermore, the amount of funding available would be limited to revenues generated since borrowing would still be restricted by PAYGO procedures.

D. Changing Both the FAA's Revenues and SpendingD. Changing Both the FAA's Revenues and SpendingD. Changing Both the FAA's Revenues and Spending

1. Add User Fees to the Current Taxes. Add User Fees to the Current Taxes. Add User Fees to the Current Taxes

<u>Definition and Example</u>: The FAA currently collects some user fees. This proposal would keep the current taxes and add some true user fees to increase the FAA's budget. The additional user fees in this proposal would be offsetting collections. The advantage of proposing user fees that are also offsetting collections is that an offsetting collection can be collected and spent without going through a traditional appropriation. Additional user fees could be aircraft certification fees or charges for the use of flight service stations.

<u>Role of Congress</u>: The FAA has the ability to collect user fees now; however, Congress could pass a specific law which could specify how the user fee (s) is created, administrated, and/or spent. If the user fee was in an appropriations bill and not permanent law, then the user fee would have to be legislated annually. The bulk of the FAA would still be funded with taxes. In addition, that portion of the FAA's budget supported with taxes would need an appropriation, and the FAA would still need to be authorized by Congress.

<u>Role of the Executive Branch</u>: Typically, the Executive Branch implements a user fee by initiating a rulemaking procedure to determine the best approach to charging and collecting the proposed user fee. If the user fee was an offsetting collection and established in permanent law, the executive branch could spend the user fee revenues without additional Congressional direction.

<u>Budget Treatment</u>: That portion of the FAA's budget supported by taxes would be under the same rules it is currently under. User fees that are offsetting collections would be part of FAA's gross budget authority and outlays. In other words, the offsetting collections (user fees)

would be counted as an addition to the FAA's appropriation level. The revenue from the user fees would most likely be limited to supporting the service the user charge is associated with.

Pros:

- This proposal would more closely associate the services the users receive with the charges the users pay.
- This proposal would provide the FAA with more funds that also would not be part of the traditional appropriations process.

Cons:

- With user fees added on top of the existing taxes, some users could potentially be over-charged for services.
- This proposal does not encourage the FAA to become more efficient.
- The majority of FAA's budget would still be subject to the discretionary budget caps.

2. Complete Replacement of the Taxes with User Fees. Complete Replacement of the Taxes with User Fees. Complete Replacement of the Taxes with User Fees

Definition and Example: All of the aviation taxes would be replaced with true user fees. Various user fee options are discussed in the Finance paper. What is important for this example is that they are true user fees and reflect the cost users impose on the system. For the purposes of this example, the FAA would still receive the General Fund contribution. Although it is the subject of debate, the General Fund contribution could possibly be replaced by user fees.

Role of Congress: Although the FAA currently has the ability to charge user fees, the FAA would also want the ability to spend the user fees. Therefore, the FAA would need the authority to collect and spend user fees. However, when drafting user fee legislation, much of the debate would focus on the definition of a true user fee. The definition is key because taxes are within the jurisdiction of the House Ways and Means Committee and the Senate Finance Committee, while true user fees are within the jurisdiction of the authorizing committees. In addition, true user fees that are established as offsetting collections are not controlled by the discretionary budget cap or traditional appropriation bills. Depending on the legislation establishing the user fees, the FAA may only need authorizing legislation and not an appropriation to spend its user fee revenues. However, the authorizing legislation could be very specific on spending the user fee revenue. Once again, issues associate with the construction of user fees are discussed in the Financing and Cost Allocation papers.

The portion of the FAA's budget supported by General Fund revenues would continue to be funded through the appropriations process and subject to discretionary budget caps.

The type of user charge determines who has the power to create them, change them, and implement them. For instance, some user charges can only be created by Congress. If that is the case, it is important to know which committees have jurisdiction over the fees. For instance, if a user charge is considered a tax, there will be seven Congressional committees (two tax-writing, two appropriating, and three authorizing) involved in overseeing one aspect or another of the FAA. If the user charge is considered a true, permanent user fee, then only three two authorizing committees would have jurisdiction over FAA. As a general rule, the more Committees involved in a user charge, the more difficult it would be to change the user charge.

Role of the Executive Branch: As discussed above, the Executive Branch typically issues a rule regarding implementation of a new user fee. The user fee revenue would have to support the services for which it is collected. However, the FAA would still have to make decisions on how to spend the funds and provide the best service for the users.

Budget Treatment: Since the aviation taxes would be eliminated, there would have to be an appropriate PAYGO offset, or waiver of the budget rules. The aviation taxes are mandatory, while user fees are discretionary under this example. Therefore, additional user fees cannot be a PAYGO offset for a cut in taxes. Although many will propose that a complementary reduction in the discretionary budget cap would be an appropriate PAYGO offset, it is not acceptable under the BEA. If such a proposal were made, the House and Senate would have to overrule or waive the BEA law.

User fees could be established as discretionary or mandatory offsetting collections. That means that the fees would be considered part of the FAA's gross budget authority and gross outlays. The FAA's authority to collect and spend user fees may be part of the annual appropriations process or in permanent law. Nevertheless, the user fees would simply fund the services they were collected to support.

Pros:

- This proposal would more closely link revenues expenditures.
- In theory, this could make FAA a more responsive and efficient agency.
- The FAA would be able to collect and spend the aviation user charges with limited Congressional involvement.

Cons:

- Part of the FAA's budget would still be supported with General Fund monies and subject to the cuts under the discretionary budget cap.
- User fees may be more difficult to collect.
- Some aviation system users believe the current taxes are fair, easy to collect, and should not be changed.
- Politically, any user fee proposal would face strong resistance by the tax-writing and appropriations committees. Such resistance would be based, at a minimum, on jurisdictional and loss-of-control issues.

E. Additional AlternativesE. Additional AlternativesE. Additional Alternatives

1. Linked Financing. Linked Financing. Linked Financing

Definition & Example: The Aircraft Owners and Pilots Association (AOPA) has developed an aviation system funding proposal known as "Linked Financing." A bill has been introduced in the House of Representatives that embodies this proposal. The Linked Financing proposal attempts to address potential FAA funding problems, while also maintaining the jurisdiction of the relevant authorizing, appropriating, and tax-writing committees.

Under the Linked Financing concept, the existing forms of user taxes would remain the same (i.e., ticket tax, cargo waybill tax, general aviation fuel taxes, and the international departure fee). The rate of each tax, however, would vary depending upon how much money Congress appropriated out of the Trust Fund to the FAA in the prior year. The key feature is that revenue collected in one fiscal year is meant to equal spending out of the Trust Fund in the previous fiscal year. For example, if the FAA's spending goes up one year, the tax rate could be adjusted upwards for the following year so that the amount collected was equal to the prior year's Trust Fund spending total. Of course, if aviation system usage increases as projected, then increasing the tax rates would only be necessary if the expected growth in revenues did not match the increase in spending during the previous fiscal year. Also, the tax rates would have upper caps or limits. If FAA spending drops, tax rates would drop automatically the following year to reflect the decrease.

The Linked Financing plan also would establish an "Annual Reserve Account" in the Aviation Trust Fund. The amount deposited each year into the Annual Reserve Account would equal any increase in revenues flowing into the Trust Fund above the revenues raised during the prior fiscal year. This deposited amount would be attributed to the prior year's increase in the excise tax rate, if any, to increased tax revenues from increased system usage, or to both factors. The revenue in the new account theoretically would be available to the appropriations committees to supplement the resources otherwise available to them within the discretionary spending cap. Spending from the Annual Reserve Account would explicitly be exempted from the discretionary spending caps, so that this cap would not limit the ability of Congress to spend the additional funds collected from users.

Role of Congress: Besides passing the underlying legislation to initiate the linked financing program, Congress would have its usual role of authorizing FAA programs and appropriating funds for FAA accounts. However, because the Secretary of the Treasury would be responsible for prescribing tax rates, the proposal may raise a constitutional issue. The Constitution explicitly gives Congress the power to raise revenues through taxation. Any delegation of that power to the executive branch might be scrutinized for potentially violating the principle of "separation of powers." Although it is not clear whether the delegation of the power in the case of Linked Financing would be unconstitutional, the fact that the Secretary's power would be limited to merely adjusting rates based upon prescribed standards and limits would work in the proposal's favor. Regardless of its constitutionality, the tax-writing committees of Congress have never made such a delegation of their powers and might be very reluctant to do so, according to the staff of the Joint Tax Committee.

Role of Executive Branch: The Secretary of the Treasury would be responsible for establishing the tax rates for each fiscal year based upon a formula set forth by Congress. Not later than September 1 of each year, the Secretary would prescribe the rates for the forthcoming fiscal year at such a level that the aggregate aviation tax revenues for the forthcoming fiscal year would equal the estimated aggregate aviation expenditures (i.e., appropriations) out of the Trust Fund from the current fiscal year.

Budget Treatment: The Linked Financing proposal presents unique questions with regard to how it would be treated under current budget rules. Therefore, like many other proposals seeking to change the way aviation revenues can be spent, it will probably be necessary to amend the BEA and/or other budget laws and procedures. Because the tax rates could vary depending upon future spending decisions, scoring of the bill would be very difficult. Under normal PAYGO procedures, any decrease in the tax rate would require an offset of an equal amount (i.e., a mandatory spending cut or a mandatory revenue increase). PAYGO procedures, however, only apply to legislation before Congress. If the Secretary of the Treasury is given the authority to decrease the tax rate without separate legislative action, then PAYGO procedures would not apply to changes in the tax rate made after passage of the bill. However, any decrease in revenues that would result from a lowered tax rate would show up as an increase in the overall federal deficit unless there is some sort of offset elsewhere in the budget.

As mentioned above, the Annual Reserve Account would be exempted from all budgetary constraints. Despite its exemption for annual deficit calculations, spending from Annual Reserve Account might increase the national debt if its budgetary treatment is not carefully constructed. In addition, without some type of waiver, exemption, or other amendment to current budget procedures, a future aviation appropriation bill might encounter scoring problems because of its effect on federal revenues in the following fiscal year.

Pros:

- Assuming that various budget and constitutional issues are resolved, the Linked Financing mechanism theoretically would be revenue neutral over the years.
- According to proponents, this proposal would give appropriators the amount of funds that is annually needed to fund the nation's aviation system while preserving traditional Congressional roles.
- Given that the Annual Reserve Account would probably grow through a natural increase in revenues derived from increased system usage, and possibly through tax increases, the appropriators may be able to spend more money on aviation programs than might otherwise be available because this account is unconstrained by budget caps and restrictions.

- Because the appropriators would still have a role in the process, spending discipline could be maintained at the FAA.
- Under this mechanism, users would have an incentive to recommend to Congress ways to reduce FAA spending since doing so would lower their taxes.
- The Trust Fund would not accrue a surplus -- something that had occurred in the past and had been heavily criticized in the aviation community.

Cons:

- As already mentioned, the tax-writing committees may be reluctant to delegate their authority to prescribe tax rates.
- Passage through Congress may be difficult as with any proposal that has significant budget scoring issues that would need to be resolved. For example, a decrease in spending by appropriators might indirectly lead to an increase in the federal deficit in a subsequent fiscal year because of the corresponding decline in tax rates.
- The budget exemptions for the Annual Reserve Account would also be criticized as a way to increase federal spending without budget constraint, thereby increasing the deficit.
- The projected growth in revenues derived from the aviation system under the current tax system have been factored into assumptions being used in the negotiations currently underway to balance the federal budget. Under Linked Financing, however, much of the growth in revenues through increased system usage would flow into the Annual Reserve Account, which is outside of budget calculations on revenue. To keep the Linked Financing structure within the constraints of any budget deal, some sort of offset or other adjustment may be necessary.
- This proposal does not in any way deal with the General Fund contribution to the budget of the FAA. It is the availability of the General Fund contribution to the FAA budget that is currently of great concern because it is likely to diminish under the caps placed on discretionary spending by the balanced budget agreement.
- If the appropriators provided the same overall amount of money to the FAA from one year to the next, but increased the General Fund contribution relative to the Trust Fund share, then tax rates would drop placing a greater strain on the federal budget. Of course, the ratio of General Fund to Trust Fund contributions is determined by authorizing legislation, which may need to be amended to accommodate this mechanism as well as many other proposals.
- The Linked Financing mechanism might have the unintended consequence of reducing tax revenues (and thereby increasing the deficit) if FAA spending is falling because of tight discretionary spending caps (at the same time the FAA's requirements are increasing). This could happen because there is no guarantee that aviation revenues are spent on the FAA. In other words, FAA spending is still subject to the vagaries of the budget and appropriations process.
- From a private sector perspective, businesses would have difficulty estimating their tax burdens in future years if the rates were variable. However, given the defined variation in the rates and a known upper cap, this may be of limited concern.

2. Multi-Year Budget. Multi-Year Budget. Multi-Year Budget

The annual appropriations process requires extensive preparation and justification at each level. It also creates a system of uncertainty that makes long-term planning very difficult. A multi-year budget may provide some funding stability and may reduce the incidence of unnecessarily detailed management oversight. In fact, the Federal Aviation Reauthorization Act of 1996 requires Congress to provide the FAA with three-year authorizations and appropriations. Whether or not the appropriating committees actually comply with this requirement for the FAA remains to be seen.

Presently, the Department of Defense (DoD) is the only federal entity that has had multi-year appropriations in the past, and those have been viewed as having limited benefits since Congress still reviews the DoD budget each year, providing updates. From the DoD point of view, they have implemented, as required, multi-year budgeting, but Congress has not. This has forced the DoD each year to do a two-year and a one-year budget, increasing the department's burden.

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