



Air Service at Kentucky's Commercial Airports

Research Report No. 390

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Air Service at Kentucky's Commercial Airports

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**Program Review and Investigations Committee
Adopted January 13, 2011**

Abstract

Significant changes in the air transportation industry include airline bankruptcies and mergers and the increased presence of low-cost carriers. Since 2000, total flights decreased by more than 25 percent at Kentucky's five commercial airports; passenger boardings and available seats each declined by nearly half. Most of the decreases were at the Cincinnati/Northern Kentucky airport. Passenger boardings over this period were also down at the Louisville and Lexington airports, but the number of flights increased at each. Kentucky's three largest airports have made proposals to facilitate the provision of incentives to increase air service. The use of airport revenues for providing incentives to airlines is generally restricted by policies and procedures of the US Federal Aviation Administration. Agreements between airports and airlines may also affect the provision of such incentives. There are numerous examples of airports, local governments, and private entities in the US providing incentives to airlines to expand or maintain air service. Cases of state governments providing incentives are less common, and only two states have ongoing programs for funding incentives for air service.

Foreword

At its June 2010 meeting, the Program Review and Investigations Committee voted to conduct a study of economic incentives for air service in Kentucky. During the course of the study, many individuals provided assistance.

Program Review staff especially thank officials from Kentucky's five commercial airports: Airport Manager Richard Roof and Marketing Director Jackie Jones of the Barkley Regional Airport; Executive Director Eric J. Frankl and Deputy Director of Air Service and Community Relations Brian Ellestad of the Blue Grass Airport; Chief Executive Officer John C. Mok, Chief Financial Officer Sheila R. Hammons, Director for Public and Government Affairs Barbara Schempf, and Chief Administrative Officer Candace S. McGraw of the Cincinnati/Northern Kentucky International Airport; Executive Director C.T. "Skip" Miller and Director of Marketing and Air Service Development Thomas Tyra of the Louisville International Airport; and Executive Director Bob Whitmer of the Owensboro-Daviess County Airport.

Also providing valuable assistance were Matt Davis, vice president, business and community advocacy, Northern Kentucky Chamber of Commerce; George M. Vredeyeld, director, and Jennifer S. Pitzer, research associate, University of Cincinnati Economics Center; Amber E. Schlabs, aeronautics business and marketing manager, Wyoming Department of Transportation; Julie A. Bordes, marketing manager, Mobile Airport Authority; and Thea Graham, manager, economic analysis, US Federal Aviation Administration.

Robert Sherman
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Contents

| | |
|--|-----|
| Summary..... | vii |
| Chapter 1: Overview of Commercial Airports | 1 |
| Major Conclusions..... | 2 |
| Suggestions From Kentucky’s Three Largest Airports | 3 |
| International Service | 5 |
| Airport Classifications | 6 |
| Commercial..... | 7 |
| General Aviation..... | 8 |
| Trends in Scheduled Flights, Passenger Boardings, and Capacity..... | 9 |
| Scheduled Flights | 9 |
| Passenger Boardings | 10 |
| Capacity | 12 |
| Destinations Served | 13 |
| Airfares..... | 14 |
| Economic Impact of Air Transportation in Kentucky | 15 |
| Cincinnati/Northern Kentucky..... | 15 |
| Louisville | 16 |
| Lexington..... | 16 |
| Statewide | 17 |
| Chapter 2: Airport Administration and Finance | 21 |
| Administration..... | 21 |
| Use Agreements | 21 |
| Restrictions on the Use of Airport Revenues | 22 |
| Sources of Revenue | 24 |
| Operating Revenues | 24 |
| Bonds..... | 26 |
| State Government..... | 26 |
| Federal Government..... | 27 |
| Airport Improvement Program..... | 27 |
| Essential Air Service Program | 27 |
| Small Community Air Service Development Program | 28 |
| Passenger Facility Charges | 29 |
| Operating Expenses | 30 |
| Chapter 3: Incentives for Provision of Air Service..... | 31 |
| Air Service Development Techniques | 32 |
| Examples of Incentives Offered by Airports, Local Governments, and Private Entities | 33 |
| Ground Services..... | 35 |
| Mobile Station Services Program..... | 35 |
| Examples of Incentives Offered by State Governments | 36 |
| Incentives for International Service | 36 |

| | |
|---|----|
| Pennsylvania..... | 36 |
| Utah..... | 37 |
| Incentives for Domestic Service | 38 |
| Florida..... | 38 |
| Ohio: Continental Airlines | 38 |
| Ohio: Skybus Airlines..... | 39 |
| North Carolina..... | 40 |
| State Incentive Programs in Operation | 41 |
| Kansas | 41 |
| Estimated Economic Impact..... | 42 |
| Wyoming | 42 |
| Proposed State Incentive Programs | 43 |
| South Carolina | 43 |
| Louisiana | 44 |
| Works Cited..... | 45 |
| Appendix A: Letter From Officials of the Kenton County Airport Board, Louisville Regional Airport Authority, and Blue Grass Airport..... | 51 |
| Appendix B: Example of an Incentive Program Offered by an Airport..... | 55 |
| Appendix C: Enacted State Incentive Programs: Kansas and Wyoming | 57 |
| Appendix D: Proposed State Programs: South Carolina and Louisiana..... | 61 |
| Appendix E: How This Study Was Conducted..... | 67 |

List of Tables

| | | |
|-----|--|----|
| 1.1 | US Commercial Airport Passenger Boardings, 2009 | 8 |
| 1.2 | General Aviation Airports in Kentucky, 2009 | 8 |
| 1.3 | Percentage Changes in Flights, Passenger Boardings, and Available Seats at Commercial Service Airports From 2000 to 2009 | 9 |
| 1.4 | Scheduled Flights at Kentucky Commercial Airports, 2000 to 2009..... | 10 |
| 1.5 | Domestic US Carrier Passenger Boardings at Kentucky Commercial Airports, 2000 to 2009..... | 11 |
| 1.6 | Available Passenger Airline Seats at Kentucky Commercial Airports, 2000 and 2009 | 12 |
| 1.7 | Percentages of Departures at Kentucky Commercial Airports to Their Top Five Destinations, January to March 2010 | 13 |
| 1.8 | Gross Domestic Product (GDP) Per Industry in Kentucky, 2007..... | 18 |
| 2.1 | Operating Revenues Per Airport, 2009..... | 25 |
| 2.2 | Airport Improvement Program Funding Per Airport, Fiscal Year 2005 to Fiscal Year 2009..... | 27 |
| 2.3 | Kentucky Community Recipients of Small Community Air Service Development Program Grants, Fiscal Year 2002 to Fiscal Year 2009 | 29 |
| 2.4 | Operating Expenses Per Airport, 2009..... | 30 |

List of Figures

| | | |
|-----|---|----|
| 1.A | Passenger Airport Classifications..... | 6 |
| 1.B | Percentage of Passenger Boardings by Airline and Airport, 2009..... | 12 |
| 1.C | Average Quarterly Airfares at the Top 100 US Airports and the Cincinnati/Northern Kentucky, Louisville, and Lexington Airports, 1995 to 2010 | 15 |

Summary

Kentucky has five airports that are defined as commercial because they provide regularly scheduled air transportation service to at least 2,500 passengers annually: Cincinnati/Northern Kentucky, Louisville International, Blue Grass (Lexington), Barkley Regional (Paducah), and Owensboro-Daviess County Regional.

As a means to provide incentives for increased air service, representatives of the Cincinnati/Northern Kentucky, Louisville, and Lexington airports recommend that state government consider adapting tax increment financing to be more appropriate for the airline industry, establishing a revolving loan fund through the issuance of bonds, and facilitating the creation by airports of separate operating units to provide support services for airlines. Their proposal is included as an appendix to the report.

The number of commercial service flights and passengers boarding planes in Kentucky has declined in recent years. Most of the decline has occurred at the Cincinnati/Northern Kentucky Airport. From 2000 to 2009, flights at the airport decreased by 35 percent and the number of passengers boarding planes fell by 54 percent. Overall, the number of flights at Kentucky's other four commercial airports increased by 8 percent over this period, but passenger boardings were down 17 percent. Nationally, the number of flights increased by 12 percent and passenger boardings were up 6 percent over this period.

With flights by its mainline carrier and its subsidiary or connection carriers, Delta Air Lines accounted for nearly 90 percent of passenger boardings at the Cincinnati/Northern Kentucky airport in 2009. At the Louisville airport, Southwest Airlines accounted for approximately one-third of passenger boardings and Delta Air Lines 27 percent. At the Lexington airport, Delta Air Lines accounted for about 57 percent of passenger boardings and US Airways 15 percent.

Federal Policies and Funding

Federal policies limit how an airport can spend its revenues. Under US Code, airport owners or operators that receive federal financial assistance cannot use airport revenues for nonairport purposes and generally cannot provide direct subsidies to air carriers. However, waiving fees or discounting landing or other fees for a limited promotional period is acceptable as long as all providers of air service at the airport are eligible to receive them. Advertising and marketing for airlines are also permitted.

Uses of airport revenue that are specifically prohibited include direct and indirect payments that do not reflect the value of services and facilities provided to an airport, general economic development, marketing and promotional activities unrelated to the airport, and inconsistently applied direct or indirect payments.

The federal government provides the largest amount of funding to airports. The largest program, the Airport Improvement Program, funds planning and capital projects. Over the 5-year period ending in fiscal year 2009, Kentucky's five commercial airports received nearly \$285 million

through the program. Grants from the Small Community Air Service Development Program can be used for incentives to improve air service to a community, but the program's funding is limited and many airports are ineligible.

Airport-airline Use Agreements

Airport-airline use agreements establish the rights, privileges, and obligations between an airport and its airline tenants. The two basic types are compensatory and residual, but many variations exist. The type of use agreement that an airport has can affect its ability to provide incentives to airlines.

Typically, residual use agreements are the most restrictive. Under this arrangement, airlines may be permitted to influence an airport's budget and how resources are spent. Airports with residual use agreements may have limited resources available to attract new or expanded air service. These agreements do typically limit financial risk for an airport because airlines are responsible for making up the difference if an airport's expenses exceed its revenues. The Cincinnati/Northern Kentucky airport has a residual use agreement with its signatory airlines.

Under compensatory use agreements, airports have a higher level of control over the financial operation of the airport but are subject to more financial risk. Airlines agree to pay certain fees and costs to the airport, but the airport is responsible for balancing its expenses should revenues fall short of what is needed. The Louisville and Blue Grass airports have compensatory use agreements.

The Paducah and Owensboro airports have short-term arrangements with each of their tenant airlines.

Incentives for Air Service

The minimum revenue guarantee establishes a base level of revenue that an airline will get for specified air service. If revenue from passengers on the guaranteed flights is insufficient to meet the agreed-upon minimum, then the airport or other entity making the guarantee is responsible for making up the shortfall. Depending on revenue from passengers, the airport or other entity may end up paying all, part, or none of the guarantee. Under a guaranteed ticket purchase program, also called a travel bank, businesses or individuals deposit funds in a bank account to be used for purchasing tickets on a specified airline over a specified time period. Cost subsidies include waivers or reductions in landing fees or terminal rent for a specified period. Airports may provide ground services for an airline. Cash subsidies can be provided that are not contingent on the airline earning a specified amount of revenue for the service being provided.

The most commonly used technique to increase or maintain air service appears to be marketing or advertising assistance by airports to promote for a specified period of time the establishment of new or expanded air service.

The report provides examples of incentives for domestic and international air service that have been offered by airports, private entities, and local governments. In some of the examples, the

incentive was successful in that the air service was maintained after the incentives ended. In other cases, the service was not maintained. Seven examples of state-funded incentive programs are examined. Incentives were for adding domestic or international flights, or for expanding specific airlines' capacity at airports. The incentives offered ranged from \$650,000 to more than \$16 million.

The exact number of state-funded incentive programs is unknown, but it appears, based on publicly available sources, that state incentives are uncommon. Kansas and Wyoming appear to have the only state programs that provide statutory guidelines and a long-term pool of state funding for incentives. Bills to establish state programs in Louisiana and South Carolina were proposed in 2010 but not enacted.

Since 2006, the Kansas legislature has appropriated nearly \$25 million for the Affordable Airfare Fund. Money from the fund and local matching contributions have been used as incentives for air service at the Wichita airport by AirTran Airways and Frontier Airlines. Since FY 2004, the Wyoming legislature has appropriated \$18 million for the Wyoming Air Service Enhancement Program. The state Aeronautics Commission decides which projects submitted by airports, for which local matching payments are required, should be funded. State payments totaling \$8.5 million have been made for incentive programs to air carriers, marketing, and facilities enhancement.

Chapter 1

Overview of Commercial Airports

This report describes air service in Kentucky and the US and describes incentives for air service that have been provided by airports, state and local governments, and private entities.

At its June 9, 2010, meeting, the Program Review and Investigations Committee voted to initiate a study of economic incentives for air service in Kentucky. Reductions in commercial air service, particularly at the Cincinnati/Northern Kentucky Airport, have raised concerns about local job losses and future economic development within the region and state. This report describes air service in Kentucky and the US and incentives for air service that have been provided by airports, local governments, private entities, and state governments.

The US airline industry has changed significantly over the past decade. There was a large decrease in the number of airline passengers after the terrorist attacks of September 11, 2001, and US airlines lost money in each of the next 5 years. Fuel prices fluctuated wildly. For example, from 2007 to 2008, the price of jet fuel, airlines' largest operating expense, increased by 60 percent, and seven smaller airlines went out of business during the first 6 months of 2008. Airlines have reduced capacity by decreasing flights and changing the mix of planes used (US. Government). Airlines have instituted fees for services such as checking bags and getting a pillow ("Airline").

Bankruptcies and mergers in recent years have restructured the industry, with major consequences for passengers and airports. US Airways filed for bankruptcy in 2004, emerged from bankruptcy in 2005, and merged with America West. Delta Air Lines and Northwest Airlines each filed for bankruptcy in 2005, emerged from bankruptcy, and merged to form a single company under the Delta name in 2008. Skybus Airlines went bankrupt and ceased operations in 2008 after receiving major financial incentive packages in two states. In 2010, Southwest Airlines agreed to buy AirTran Airways, and United Airlines and Continental Airlines merged.

The impacts of the Skybus bankruptcy and the United-Continental merger are discussed in Chapter 3 of this report. Delta Air Lines' impact on the Cincinnati/Northern Kentucky airport in recent years is well known. The dramatic reductions in the numbers of flights and passengers there are similar to earlier changes at St. Louis Lambert Airport in Missouri and Pittsburgh International Airport in Pennsylvania. TWA made St. Louis its hub in 1982. After

American Airlines purchased TWA in 2001 and began consolidating routes, the airport's hub status has been downgraded repeatedly ("Lambert"). It is no longer an American hub, and the airline now has nonstop service to only six cities from Lambert ("Non Stop"). The number of boardings of commercial passengers at the airport has declined from more than 15 million in 2000, when Lambert was the 17th busiest airport in the country, to just more than 6 million in 2009 (US. Federal. "Passenger").

In 2001, US Airways had hundreds of daily flights from its Pittsburgh hub to domestic and international destinations. After unsuccessfully pressuring the airport to reduce landing fees and lease payments, the airline began to move traffic to hubs in other cities. Pittsburgh has been gradually downgraded from a primary hub to a secondary hub to a focus city, and it is now not even a focus city ("US Airways"). As of August 2010, US Airways was still the airport's largest carrier, but with only 42 daily flights to nine US cities, all but two on the East Coast ("Status"). The number of boardings of commercial passengers at the airport has decreased from just under 10 million in 2000 to just under 4 million in 2009 (US. Federal. "Passenger").

Major Conclusions

This report has six major conclusions.

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1. As a means to provide incentives for increased air service, representatives of the Cincinnati/Northern Kentucky, Louisville, and Lexington airports propose that state government consider adapting tax increment financing to be more appropriate for the airline industry, consider establishing a revolving loan fund through the issuance of bonds, and consider facilitating the creation by airports of separate commercial operating units to provide support services for airlines.
2. Over the past decade, the air transportation industry has undergone significant changes including airline bankruptcies, airline mergers, and the increased presence of low-cost carriers.

3. For Kentucky's five commercial airports, from 2000 to 2009 total flights decreased by more than 25 percent, and the number of passenger boardings and available seats each declined by nearly half. Most of the decreases were at the Cincinnati/Northern Kentucky airport. Passenger boardings over this period were down approximately 18 percent at the Louisville airport and 11 percent at the Lexington airport, but the number of flights increased at each of them.
4. Policies and procedures of the Federal Aviation Administration restrict the use of airport revenues for the purpose of providing incentives to airlines.
5. Agreements between airports and airlines can affect an airport's ability to provide incentives to airlines.
6. There are numerous examples of airports, local governments, and private entities providing incentives to airlines to expand or maintain air service. Cases of state governments providing incentives are less common. Only Kansas and Wyoming have ongoing state programs for funding incentives for air service.

The remainder of this chapter summarizes the proposals from the Cincinnati/Northern Kentucky, Louisville, and Lexington airports; provides an overview of airport classifications and relevant terms; provides background statistics on airports and air service; describes airport finances; and summarizes material on the economic impact of airports and air service.

Suggestions From Kentucky's Three Largest Airports

Representatives of the Cincinnati/Northern Kentucky, Louisville, and Lexington airports have submitted three suggestions to benefit commercial airports in Kentucky and the state's economy: establish a tax increment financing program for development of air service, establish a revolving loan fund, and allow airport boards to establish separate commercial operating units to provide services to airlines at a lower cost.

Representatives of the Cincinnati/Northern Kentucky, Louisville, and Lexington airports have submitted three suggestions designed to benefit commercial airports in Kentucky and the state's economy. The letter with the suggestions is included as Appendix A to this report. The suggestions are to

- establish a tax increment financing program for development of air service,
- establish a revolving loan fund, and
- allow airport boards to establish separate commercial operating units to provide services to airlines at a lower cost.

Implementing these suggestions would likely require policy changes by the General Assembly.

Tax increment financing (TIF) permits local entities to use future gains in tax revenues that would be generated by new development in a specified area. For example, an economic development project would increase the value of real estate, which in turn would produce increased property tax revenues. The "tax increment" is

the difference in what tax revenues are with the new development compared to what they would have been without the development. The incremental revenues are used to finance debt to create the infrastructure needed for the development.

The governing statutes KRS Chapter 65 and KRS Chapter 154 define whether and how tax increment financing may be used, such as which entities are eligible to participate, what types of tax revenues can be considered as incremental, and minimum capital requirements, which range from \$10 million to \$200 million depending on the type of state TIF program being used.

In their proposal, the airports note that the three state TIF programs do not provide the appropriate incentives to promote new airline service. The airports suggest that the TIF statutes be changed in terms of the minimum capital requirement, that TIF revenues not be restricted to funding only capital costs, and that the tax revenues that can be pledged to support a TIF district be expanded to include taxes generated by the airline industry such as fuel taxes.

It is unknown how much additional revenue an increase in air service would create through higher aviation fuel tax receipts, but KRS 144.132 caps the amount that an air carrier pays in sales and use tax on aviation fuel at \$1 million per fiscal year. Additional service by a carrier that is already at the \$1 million limit would not increase revenue from aviation fuel taxes. For any carrier below the \$1 million cap, the amount of additional aviation fuel tax receipts generated by new service would be \$1 million minus the amount of tax paid before the new service was initiated.

The second proposal is that state government establish a revolving loan fund by issuing bonds. Specifically,

[t]hese funds would be held in an account for air service development and enhancement purposes only. An initial amount as low as \$5 million could have positive benefits. A maximum amount each airport could access would need to be established. The loan made would carry zero interest and would require a repayment over a relatively short term like 5 years.

According to the proposal, eligible expenses could include purchasing ground support equipment; purchasing marketing items such as newspaper, TV and radio advertising; and funding abatements of landing fees and terminal leases for a period of time.

There is precedent for state funds for development of air service. Programs are in operation in Kansas and Wyoming. Bills were proposed but not enacted in 2010 to create programs in South Carolina and Louisiana.

The third proposal is for the establishment of separate commercial operating units to perform aeronautical services such as baggage and cargo handling and provide equipment and space for airlines as an incentive for new routes. The airports propose that the services could be provided at a lower cost through a private company instead of governmental employees subject to statutes related to the Kentucky Retirement Systems.

It is unknown whether under existing law airport authorities could create private companies whose employees would not be part of the Kentucky Retirement Systems.

International Service

It was also requested that the committee's assessment include the economic value of international air service to Kentucky and that supporting international service be part of any overall program. According to estimates by airport and airline officials and consultants, the annual economic impact of an international flight ranges from more than \$60 million to more than \$200 million.

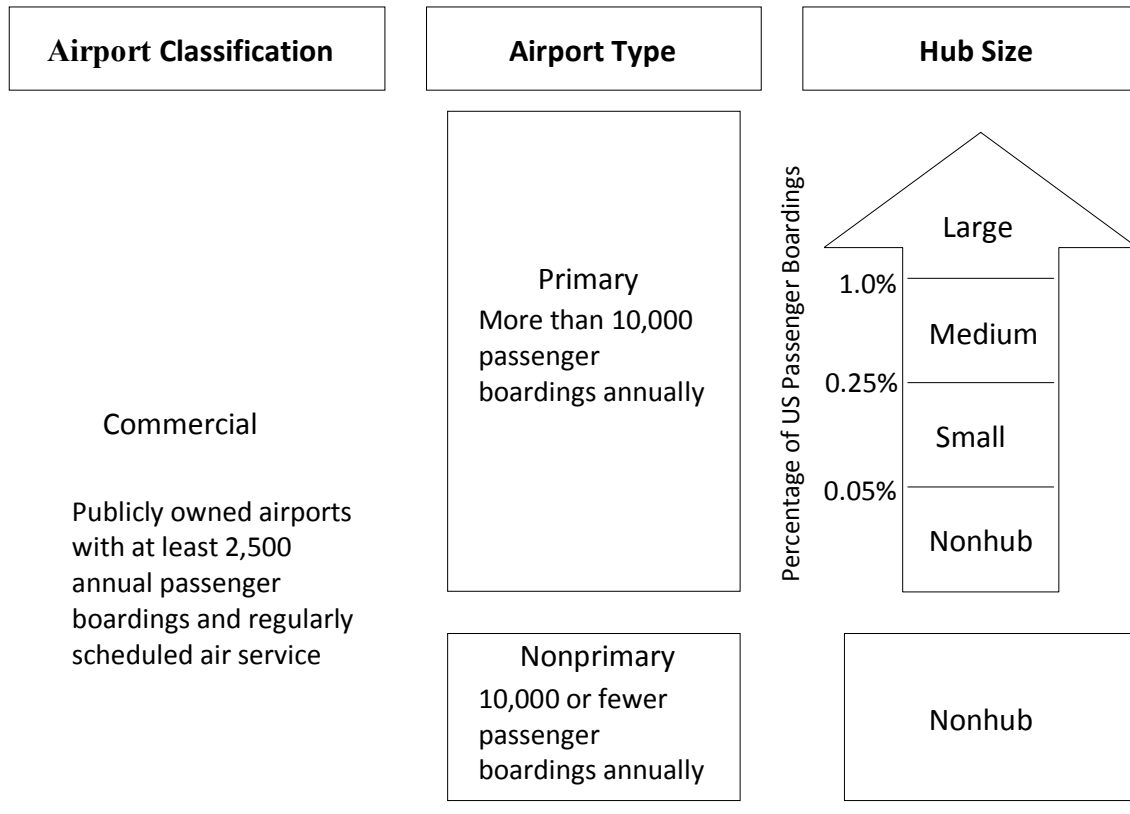
The letter from the three airports also requested that the committee's assessment include the economic value of international air service to Kentucky and that supporting international service be part of any overall program.

As described later in this chapter, there are studies that estimate the overall impact of airports and air service with documentation as to how the estimates were derived. Program Review staff found no such studies that would specifically assess the economic impact of international service. The sources of the economic impact of nonstop international flights that staff were able to identify were airport and airline officials and consultants to them. Some estimates were for existing flights; some were for potential flights. Estimates varied significantly. A typical claim is approximately \$100 million, as in San Diego, California, for example (Geresma). The lowest claimed annual economic impact that Program Review staff found was "over \$60 million" for an existing nonstop flight between Portland, Oregon, and Tokyo, Japan (Read). The highest estimates of annual economic impact were \$156 million for a flight from San Diego to London, England; \$180 million for a flight from Dallas/Fort Worth, Texas, to Beijing, China; \$238 million for a flight from Phoenix, Arizona, to London; and \$255 million for a flight from Nashville, Tennessee, to London ("DFW"; "International"). Of these four, only the Phoenix flight is in operation.

Airport Classifications

Passenger airports are officially classified according to the characteristics shown in Figure 1.A.

Figure 1.A
Passenger Airport Classifications



Source: Program Review staff’s depiction based on US Code and an adaptation of an FAA diagram (US. Federal. “Airport”).

Commercial

Kentucky has five commercial airports: Cincinnati/Northern Kentucky, Louisville International, Blue Grass (Lexington), Barkley Regional (Paducah), and Owensboro-Daviess County Regional.

Commercial service airports have at least 2,500 passengers annually and regularly scheduled air service. General aviation airports generally do not have regularly scheduled service. In Kentucky, there were 5 commercial and 53 general aviation airports in 2009.

A commercial airport is defined as a publicly owned airport with at least 2,500 passenger boardings—also referred to as enplanements—each year and with regularly scheduled air service.¹ Commercial airports with at least 10,000 passenger boardings annually are classified as primary airports; those with fewer than 10,000 passengers are nonprimary (US. Federal. “Airport”). Based on passenger boardings for 2009, Kentucky’s five commercial airports were primary.

The term “hub” is commonly used to mean an airline’s operation of a network of flights at a particular airport, such as Delta Air Lines at Hartsfield Airport in Atlanta, Georgia. Technically, however, it means the percentage of passenger boardings at an airport relative to the US total. This report uses the latter classification. Depending on the percentage of passenger boardings, an airport is classified as a large, medium, or small hub or as a nonhub.² Based on this method, for 2009, Cincinnati/Northern Kentucky is a medium hub, Louisville and Lexington are small hubs, and Paducah and Owensboro are nonhubs.

In 2009, there were 491 commercial airports in the US with nearly 700 million passenger boardings. Twenty-nine large hubs had nearly 70 percent of passenger boardings.

Table 1.1 shows the numbers of commercial airports and passenger boardings by type of airport in the US for 2009. There were 491 commercial airports with nearly 700 million passenger boardings. Twenty-nine large hubs had nearly 70 percent of passenger boardings. Medium hubs had nearly 19 percent of passenger boardings. Small hubs had just more than 8 percent. Nearly one-half of the airports were primary nonhubs, but these airports had only 3 percent of passenger boardings.

¹ Passenger boardings/enplanements typically mean revenue passenger boardings in the US, which includes passengers who continue on an international flight that stops at a US airport. The number of passenger boardings at an airport will be less than the number of passengers who go through the airport.

² A large hub has 1 percent or more of annual US commercial passenger boardings, a medium hub has at least 0.25 percent but less than 1 percent, and a small hub has at least 0.05 percent but less than 0.25 percent. The remaining primary airports and all commercial airports with fewer than 10,000 annual commercial passenger boardings are nonhubs (US. Federal. “Airport”).

Table 1.1
US Commercial Airport Passenger Boardings
2009

| | Hub Size | Airports | % of Total | Passenger Boardings | % of Total |
|-------------------|---------------------|-----------------|-----------------------|--------------------------------|-----------------------|
| Primary | Large | 29 | 5.9% | 484,785,812 | 69.7% |
| | Medium | 36 | 7.3 | 131,835,174 | 18.9 |
| | Small | 71 | 14.5 | 57,342,955 | 8.2 |
| | Nonhub | 226 | 46.0 | 21,319,315 | 3.1 |
| Nonprimary | | 129 | 26.3 | 628,506 | 0.1 |
| | Total | 491 | 100.0% | 695,911,762 | 100.0% |

Source: Compiled by Program Review staff from US. Federal. "Passenger."

General Aviation

There are more than 2,500 general aviation airports in the United States, by far the most common type of airport that is open to the public (US. Federal. *National*). General aviation airports are not specifically defined in the US Code but are typically considered by the Federal Aviation Administration to be publicly owned airports without scheduled air service. Table 1.2 lists the cities for Kentucky's 53 general aviation airports as of 2009.

Table 1.2
General Aviation Airports in Kentucky
2009

| | | | | |
|----------------|---------------|--------------|----------------|---------------|
| Ashland | Frankfort | Hopkinsville | Mayfield | Russellville |
| Bardstown | Fulton | Irvine | Middlesboro | Somerset |
| Bowling Green | Georgetown | Jackson | Monticello | Sparta |
| Cadiz | Gilbertsville | Jamestown | Morehead | Springfield |
| Campbellsville | Glasgow | Leitchfield | Mount Sterling | Stanton |
| Cynthiana | Greenville | Lewisport | Murray | Sturgis |
| Danville | Hardinsburg | Liberty | Pikeville | Tompkinsville |
| Elizabethtown | Harlan | London | Pine Knot | West Liberty |
| Falls of Rough | Hartford | Louisville | Prestonsburg | Williamsburg |
| Falmouth | Hazard | Madisonville | Princeton | |
| Flemingsburg | Henderson | Marion | Richmond | |

Source: US. Federal. *National*. Owensboro-Daviess County Regional Airport was listed in the source report as a general aviation airport. Based on passenger boardings in 2009, it qualifies as a commercial, primary airport and is defined as such in this report.

Trends in Scheduled Flights, Passenger Boardings, and Capacity

Airports are frequently measured and compared by the number of passengers, flights, and seat capacity. This section describes the annual number of passenger boardings at US and Kentucky airports, as well as the annual number of flights and available airline seats at Kentucky’s commercial airports.

As shown in Table 1.3, from 2000 to 2009 the number of scheduled flights decreased by more than one-third at the Northern Kentucky airport but increased nationally and for Kentucky’s other commercial airports as a group. Passenger boardings increased nationally and at the Owensboro airport, but decreased at the remaining four commercial airports in Kentucky. The number of available seats declined nationally and at each of Kentucky’s commercial airports.

**Table 1.3
 Percentage Changes in Flights, Passenger Boardings, and Available Seats
 at Commercial Service Airports From 2000 to 2009**

| | US | Kentucky | |
|---------------------|-------|----------------------------------|--|
| | | Cincinnati/ Northern Kentucky | Lexington, Louisville, Owensboro, Paducah |
| Flights | + 12% | - 35% | + 8% |
| Passenger boardings | + 6 | - 54 | - 17 |
| Available seats | - 9 | - 56 | - 26 |

Source: US. Dept. Bureau. “Flights”; US. Dept. Federal. “Passenger”; US. Dept. Bureau. Air.

Scheduled Flights

The number of scheduled flights rose by almost 12 percent at US airports from 2000 to 2009. The number of scheduled flights fell by 26 percent at Kentucky’s commercial airports over the same period.

Nationally, the annual number of scheduled flights increased by almost 12 percent from 2000 to 2009 (US. Dept. Bureau. “Flights”). In Kentucky, however, the annual number of scheduled flights at commercial airports fell by more than 26 percent. As shown in Table 1.4, most of the decline occurred at the Cincinnati/Northern Kentucky airport, which lost 35 percent, or approximately 50,000 scheduled flights. The number of flights at the Louisville airport varied by year, but the number for 2009 was 1.6 percent higher than in 2000. Annual numbers were up and down at the Lexington airport as well, but the 2009 figure was more than 25 percent higher than in 2000.

Table 1.4
Scheduled Flights at Kentucky Commercial Airports
2000 to 2009

| Year | Cincinnati/ Northern Kentucky | Louisville | Lexington | Paducah | Owensboro | Total |
|---------------------------|--|-------------------|------------------|----------------|------------------|--------------|
| 2000 | 155,090 | 28,734 | 9,839 | 1,163 | n/a | 194,826 |
| 2001 | 145,046 | 28,653 | 9,368 | 681 | n/a | 183,748 |
| 2002 | 199,096 | 30,799 | 11,382 | 579 | 225 | 242,081 |
| 2003 | 217,650 | 35,246 | 16,240 | 2,305 | 914 | 272,355 |
| 2004 | 226,950 | 33,528 | 15,726 | 1,986 | 660 | 278,850 |
| 2005 | 222,303 | 36,562 | 15,218 | 1,927 | 744 | 276,754 |
| 2006 | 159,536 | 31,842 | 14,243 | 1,380 | 574 | 207,575 |
| 2007 | 153,055 | 34,648 | 14,047 | 1,080 | 120 | 202,950 |
| 2008 | 133,480 | 32,265 | 13,923 | 1,058 | 10 | 180,736 |
| 2009 | 100,427 | 29,199 | 12,316 | 911 | 361 | 143,214 |
| % Change, 2000 to 2009 | -35.2% | 1.6% | 25.2% | -21.7% | n/a | -26.5% |

Source: US. Dept. Bureau. "Flights."

Passenger Boardings

Passenger boardings at US commercial airports grew by 6 percent from 2000 to 2009 but declined by 47 percent in Kentucky. In Kentucky, there were 6.4 million fewer boardings in 2009 than in 2000, with 6 million of the decrease occurring at the Cincinnati/Northern Kentucky airport. Passenger boardings were also down at the Louisville, Lexington, and Paducah airports.

Between 2000 and 2009, the number of passenger boardings at US commercial airports grew by 6 percent. Passenger boardings at Kentucky's commercial airports fell by nearly 47 percent over the same period.

Table 1.5 shows the number of domestic passenger boardings for Kentucky commercial airports from 2000 to 2009. Overall, there were 6.4 million fewer passenger boardings in 2009 than in 2000, with 6 million of the decrease occurring at the Northern Kentucky airport. Passenger boardings were down approximately 18 percent in Louisville, 11 percent in Lexington, and 40 percent in Paducah. Passenger boardings at Owensboro-Daviess County were slightly higher in 2009 than in 2000, but scheduled commercial service was not available for every year.

Table 1.5
Domestic US Carrier Passenger Boardings at Kentucky Commercial Airports
2000 to 2009

| Year | Cincinnati/ Northern Kentucky | Louisville | Lexington | Paducah | Owensboro | Total |
|---------------------------|--|-------------------|------------------|----------------|------------------|--------------|
| 2000 | 11,223,966 | 1,974,269 | 507,334 | 30,883 | 10,034 | 13,746,486 |
| 2001 | 8,586,907 | 1,876,499 | 440,797 | 31,400 | 6,868 | 10,942,471 |
| 2002 | 10,316,170 | 1,740,526 | 477,173 | 29,768 | 8,671 | 12,572,308 |
| 2003 | 10,449,930 | 1,656,609 | 581,899 | 32,839 | 6,635 | 12,727,912 |
| 2004 | 10,864,547 | 1,720,377 | 582,328 | 32,971 | 2,850 | 13,203,073 |
| 2005 | 11,277,068 | 1,862,017 | 536,000 | 33,981 | 3,611 | 13,712,677 |
| 2006 | 7,984,074 | 1,836,260 | 504,787 | 26,742 | 0 | 10,351,863 |
| 2007 | 7,728,069 | 1,912,495 | 520,760 | 24,537 | 0 | 10,185,861 |
| 2008 | 6,648,600 | 1,845,317 | 496,384 | 21,654 | 103 | 9,012,058 |
| 2009 | 5,194,214 | 1,622,804 | 450,464 | 18,542 | 10,720 | 7,296,744 |
| % Change, 2000 to 2009 | -53.7% | -17.8% | -11.2% | -40.0% | 6.8% | -46.9% |

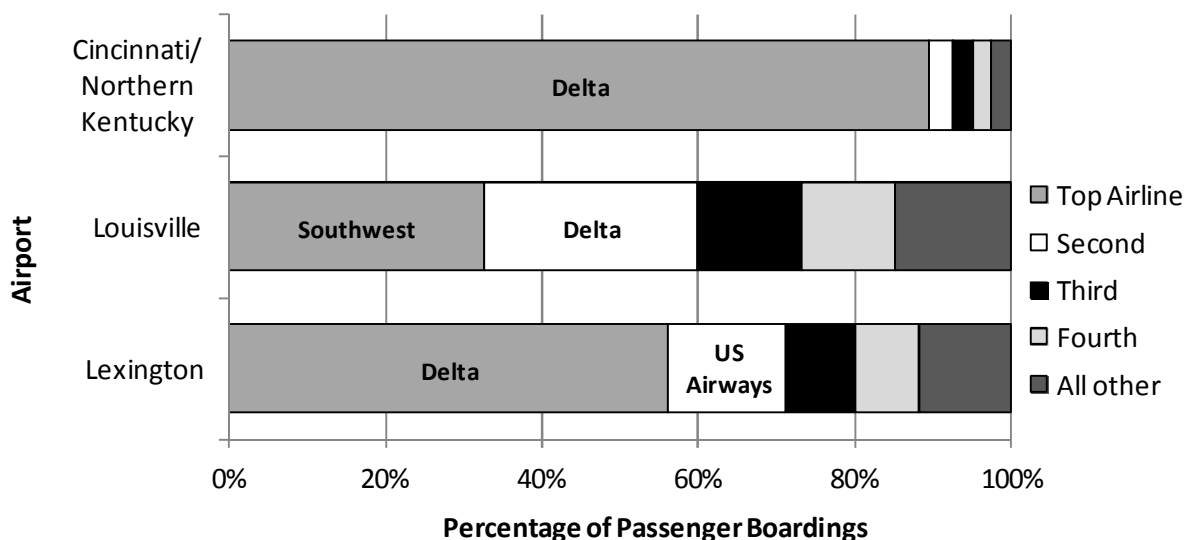
Source: US. Federal. "Passenger."

At the Cincinnati/Northern Kentucky airport, Delta Air Lines accounted for nearly 90 percent of passenger boardings in 2009. At the Louisville airport, Southwest Airlines accounted for approximately one-third of passenger boardings and Delta Air Lines another 27 percent. At the Lexington airport, Delta Air Lines accounted for about 57 percent of passenger boardings and US Airways 15 percent.

Airports in Cincinnati/Northern Kentucky, Louisville, and Lexington are each served by several airlines, but the distribution of passenger boardings by airline varies. Figure 1.B shows the percentage of passenger boardings for each airport's top four airlines. In the figure, service by a mainline provider includes its own flights but also service provided by subsidiary or connection carriers. For example, passenger boardings on the Delta subsidiary Comair are counted as boardings for Delta Air Lines.

At the Cincinnati/Northern Kentucky airport, Delta Air Lines accounted for nearly 90 percent of passenger boardings in 2009. At the Louisville airport, Southwest Airlines accounted for approximately one-third of passenger boardings and Delta Air Lines another 27 percent. At the Lexington airport, Delta Air Lines accounted for about 57 percent of passenger boardings and US Airways 15 percent.

Figure 1.B
Percentage of Passenger Boardings by Airline and Airport
2009



Source: Program Review staff analysis of US. Dept. Bureau. Air.

Capacity

From 2000 to 2009, the number of available passenger airline seats at Kentucky's commercial airports declined by 9.5 million, or almost 50 percent. Nationally, the number of available passenger airline seats declined by about 9 percent.

As shown in Table 1.6, from 2000 to 2009 the number of available passenger airline seats at Kentucky's commercial airports declined by almost 50 percent. In 2000, there were 18.7 million available seats, but by 2009 there were 9.5 million. The Northern Kentucky airport had the largest decrease, losing approximately 8.2 million seats, a drop of almost 56 percent. Over the same period, available seats were down by nearly 29 percent in Louisville and more than 18 percent in Lexington. Paducah was the only Kentucky commercial airport for which the number of available seats was higher than in 2000, up 12.9 percent. Nationally, the number of available passenger seats declined by 9 percent from 2000 to 2009.

Table 1.6
Available Passenger Airline Seats at Kentucky Commercial Airports
2000 and 2009

| Airport | 2000 | 2009 | Percent Change |
|------------------------------|------------|-----------|----------------|
| Cincinnati/Northern Kentucky | 14,756,120 | 6,556,243 | -55.6% |
| Louisville | 3,159,088 | 2,248,355 | -28.8 |
| Lexington | 786,296 | 642,952 | -18.2 |
| Paducah | 27,581 | 31,148 | 12.9 |
| Owensboro | n/a | 14,106 | n/a |
| Total | 18,729,085 | 9,492,804 | -49.3% |

Source: Program Review staff's analysis of US. Dept. Bureau. Air.

Destinations Served

In the first quarter of 2010, service was provided to 93 destinations by the Cincinnati/Northern Kentucky airport, 38 destinations by the Louisville airport, and 21 by the Lexington airport. The Paducah and Owensboro airports each provided service to two destinations.

Table 1.7 shows the top five flight destinations for scheduled passenger/cargo service from each commercial airport in Kentucky for the first quarter of 2010. Among the three largest airports, the top five destinations accounted for approximately 23 percent of the departures at Cincinnati/Northern Kentucky, 43 percent at Louisville, and 70 percent at Lexington. Only Chicago, Illinois, (8.2 percent) accounted for more than 4 percent of departures at Cincinnati/Northern Kentucky. In contrast, 30 percent of Louisville departures were to Chicago (two airports) and Dallas/Fort Worth, Texas; 39 percent of Lexington departures were to Atlanta, Georgia, and Charlotte, North Carolina. Paducah and Owensboro each had flights to only two cities.

Table 1.7
Percentages of Departures at Kentucky Commercial
Airports to Their Top Five Destinations
January to March 2010

| Destination | Cincinnati/ Northern Kentucky | Louisville | Lexington | Paducah | Owensboro |
|------------------------------|--|-------------------|------------------|----------------|------------------|
| Atlanta | 3.3% | | 23.6% | | |
| Charlotte | 3.7 | 7.5% | 15.4 | | |
| Chicago (Midway) | | 5.2 | | | |
| Chicago (O'Hare) | 8.2 | 12.8 | | 54.2% | |
| Cincinnati/Northern Kentucky | | | 11.6 | | |
| Dallas Fort Worth | 4.0 | 12.0 | 9.0 | | |
| Detroit | | | 10.8 | | |
| Houston (Bush) | | 5.9 | | | |
| Memphis | | | | 45.8 | |
| Nashville | | | | | 87.0% |
| Orlando (Sanford) | | | | | 13.0 |
| Philadelphia | 3.5 | | | | |
| Total | 22.7% | 43.4% | 70.4% | 100.0% | 100.0% |

Note: Data reflect scheduled passenger/cargo service that includes at least one passenger. For the Paducah airport, a single flight to Peoria, Illinois, was excluded.

Source: Program Review staff's analysis of US. Dept. Bureau. Air.

Airfares

Since 1995, domestic fares at the Northern Kentucky airport consistently exceeded the national average. Lexington fares have also consistently been higher than average, but not by as much. Louisville fares have mostly been below the national average over this period.

Figure 1.C shows the quarterly average domestic airfares at the Cincinnati/Northern Kentucky, Louisville, and Lexington airports from 1995 to 2010 compared to average fares at the top 100 airports in the US based on passenger boardings.³ For the first quarter of 2010, the average domestic airfare was \$328 for the US, \$404 for Northern Kentucky, \$341 for Louisville, \$458 for Lexington, \$480 for Paducah, and \$117 for Owensboro (US. Dept. Bureau. "Passenger")

Domestic fares at the Northern Kentucky airport consistently exceeded the national average for this period. Depending on the quarter, its average fare was \$41 to \$248 higher than the national average. As of the first quarter of 2010, Cincinnati/Northern Kentucky's average domestic fare was still higher than the US average, but the difference—\$76—was smaller than usual.

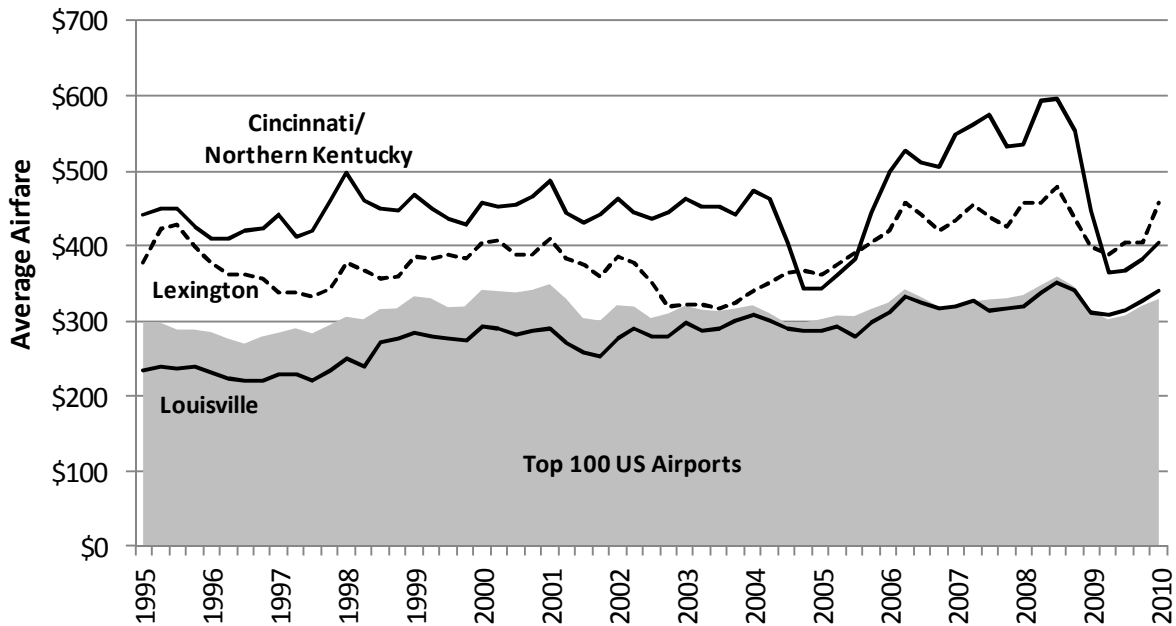
The average domestic fare from Lexington has also consistently been higher than the US average, but not by as much as at Northern Kentucky. The smallest difference was \$4 higher; the largest difference was \$141 higher.

Though the recent trend for the average domestic fare for the Louisville airport is up, its fares were below average for nearly every quarter. The most the Louisville fare was above the US average was \$13; the most below average was \$64.

They are not shown in the figure, but average airfares for the Paducah and Owensboro airports have generally exceeded the national average by 20 to 40 percent, although airfares at the Owensboro airport declined in 2009.

³ Average airfares are based on total ticket value, which includes the price charged by the airline plus taxes and fees paid at the time of purchase, but exclude baggage and other fees that are paid at the airport or on board the aircraft. Factors such as the length of a flight and the destination may affect fares (US. Dept. Bureau. About).

Figure 1.C
Average Quarterly Airfares at the Top 100 US Airports and the Cincinnati/Northern Kentucky, Louisville, and Lexington Airports 1995 to 2010



Source: Program Review staff analysis of US. Dept. Bureau. "Passenger."

Economic Impact of Air Transportation in Kentucky

The precise current economic impact of the three largest commercial airports in Kentucky is unknown. The most recent impact studies are summarized below. The statistics cited should not be interpreted as comparisons of the economic effects of the three airports. The research methods used to make the estimates are not exactly the same, and the estimates were for different years.

Cincinnati/Northern Kentucky

A 2005 study by the University of Cincinnati, based on 2003 data, estimated the annual economic impact of the Cincinnati/Northern Kentucky airport as \$4.5 billion and 56,000 jobs. The economic impact includes direct expenditures, but most of the impact comes from estimates of indirect and induced expenditures.

A 2005 study by the University of Cincinnati Economics Center, based on 2003 data, estimated the annual economic impact of the Cincinnati/Northern Kentucky airport as \$4.5 billion and 56,000 jobs. Of the total estimated impact, day-to-day operations of the airport accounted for \$2.9 billion in impact and more than 35,000 jobs through compensation to employees and purchases from local businesses. Construction accounted for \$550 million and nearly 5,000 jobs of the total estimated impact. The third major component of the estimated impact was the more than \$1 billion and 15,500 jobs generated by air travelers visiting the area.

The economic impact includes direct expenditures, but most of the impact comes from estimates of indirect and induced expenditures. Indirect expenditures are purchases of local resources to produce the goods and services used by the airport, the subsequent purchases needed to produce those resources, and so on. An example of a direct expenditure would be the wages of an employee of a business directly related to the airport. The induced impact is the household spending of employees and suppliers of the airport (University 25).

It could not be determined from the report how much of the economic impact was for Kentucky. The estimated economic impact was for the Cincinnati Metropolitan Statistical Area, which consists of seven counties in Kentucky, five counties in Ohio, and three counties in Indiana. The report does document the employment impact by place of residence for three counties. Residents of Hamilton County, Ohio, held 42.4 percent of the jobs, residents of Boone County, Kentucky, held 13.7 percent, and residents of Kenton County, Kentucky, held 13.2 percent (University 24).

Louisville

A study by the University of Louisville estimated the economic impact in 2008 of the Louisville International Airport and Bowman Field as \$6.6 billion and more than 64,000 jobs. The estimate comprises direct, indirect, and induced expenditures.

A 2009 study by the University of Louisville Urban Studies Institute estimated the economic impact in 2008 of the Louisville International Airport and Bowman Field, a general aviation airport, as \$6.6 billion and more than 64,000 jobs. Of the total estimated impact, the recurring economic impact was estimated to be \$5.7 billion and more than 55,000 jobs. Construction accounted for \$923 million and nearly 9,000 jobs of the total estimated impact for 2008. The estimate is made up of direct, indirect, and induced expenditures. A major factor in the impact of the Louisville International Airport is that 4.3 million pounds of cargo was handled at the airport in 2008, third highest among North American airports (Louisville). Based on the summary of the report, it could not be determined how much of the reported economic impact was for Kentucky.

Lexington

The most recent impact study of the Lexington airport is a decade old. A study by the University of Kentucky, based on 1999 data, estimated the annual impact of the Lexington airport as \$134.2 million and 1,760 jobs.

The most recent study of the economic impact of the Lexington airport is a decade old. The 2001 study by the University of Kentucky Center for Business and Economic Research, based on data for 1999, estimated the annual economic impact of Blue Grass Airport as more than \$134 million and 1,760 jobs. Most of the total, \$116 million and 1,380 jobs, was generated by the airport

itself. The remainder came from spending by travelers who came to the region due to the presence of the airport. The overall estimate is made up of direct, indirect, and induced expenditures (Thompson). There is no indication in the report that the impact of airport-related construction was measured.

Statewide

A report from the US Federal Aviation Administration estimates the total economic impact for civil aviation in Kentucky in 2007 was \$13.8 billion.

A 2009 report from the US Federal Aviation Administration estimates the economic impact of civil aviation for all states. The total estimated economic impact for civil aviation in Kentucky in 2007 was nearly \$13.8 billion (US. Federal. *The Economic*, and “The Economic”). The total includes the estimated direct, indirect, and induced impact. Total estimated employment was 109,110 jobs. Total estimated payroll was nearly \$3.4 billion. These numbers include commercial air service; airport operations; general aviation; air couriers; and manufacture of aircraft, aircraft engines, and parts. Commercial air service accounted for 60 percent of the total economic impact, 54 percent of total jobs, and 50 percent of payroll (US. Federal. “The Economic”).

According to the US Bureau of Economic Analysis, the air transportation industry accounted for \$698 million of gross domestic product, 0.5 percent of the state total, in Kentucky in 2007. This number does not include indirect and induced economic effects. The air transportation category does not include air couriers.

Because the reports cited previously in this chapter include the direct, indirect, and induced economic effects, the reported numbers are significantly different from the direct measure of gross domestic product (GDP) for the industry. Table 1.8 shows GDP by industry for Kentucky in 2007. According to this measure, which does not include air couriers, air transportation accounted for \$698 million of GDP, 0.5 percent of the state total. By not including the indirect and induced effects and by counting related businesses (airport rental cars, for example) in separate categories, this measure underestimates the total impact of air transportation. That would be true for other industries as well, so GDP per industry is a means for making approximate comparisons of the impact of different industries on the state’s economy. The table can be used to see which industries have similar, more, or less impact on Kentucky’s GDP compared to air transportation.

Table 1.8
Gross Domestic Product (GDP) Per Industry in Kentucky
2007

| Industry | GDP (in millions of dollars) | % of State GDP |
|--|---|---------------------------------|
| Agriculture, forestry, fishing, and hunting | \$2,619 | 1.7% |
| Crop and animal production (farms) | 2,142 | 1.4 |
| Forestry, fishing, and related activities | 477 | 0.3 |
| Mining | 3,533 | 2.3 |
| Oil and gas extraction | 210 | 0.1 |
| Mining, except oil and gas | 3,078 | 2.0 |
| Support activities for mining | 245 | 0.2 |
| Utilities | 2,414 | 1.6 |
| Construction | 5,982 | 3.9 |
| Manufacturing: Durable goods | 17,168 | 11.3 |
| Wood product manufacturing | 677 | 0.4 |
| Nonmetallic mineral product manufacturing | 929 | 0.6 |
| Primary metal manufacturing | 3,163 | 2.1 |
| Fabricated metal product manufacturing | 1,713 | 1.1 |
| Machinery manufacturing | 1,698 | 1.1 |
| Computer and electronic product manufacturing | 572 | 0.4 |
| Electrical equipment and appliance manufacturing | 1,131 | 0.7 |
| Motor vehicle, body, trailer, and parts manufacturing | 5,902 | 3.9 |
| Other transportation equipment manufacturing | 602 | 0.4 |
| Furniture and related product manufacturing | 328 | 0.2 |
| Miscellaneous manufacturing | 452 | 0.3 |
| Manufacturing: Nondurable goods | 11,776 | 7.7 |
| Food product manufacturing | 3,983 | 2.6 |
| Textile and textile product mills | 119 | 0.1 |
| Apparel manufacturing | 149 | 0.1 |
| Paper manufacturing | 1,336 | 0.9 |
| Printing and related support activities | 870 | 0.6 |
| Petroleum and coal products manufacturing | 628 | 0.4 |
| Chemical manufacturing | 3,268 | 2.1 |
| Plastics and rubber products manufacturing | 1,423 | 0.9 |
| Wholesale trade | 9,661 | 6.4 |
| Retail trade | 10,468 | 6.9 |
| Transportation and warehousing, excluding Postal Service | 7,831 | 5.1 |
| Air transportation | 698 | 0.5 |
| Rail transportation | 940 | 0.6 |
| Water transportation | 194 | 0.1 |
| Truck transportation | 2,046 | 1.3 |
| Transit and ground passenger transportation | 113 | 0.1 |
| Pipeline transportation | 129 | 0.1 |
| Other transportation and support activities | 2,808 | 1.8 |
| Warehousing and storage | 902 | 0.6 |

| Industry | GDP (in millions of dollars) | % of State GDP |
|---|---|---------------------------|
| Information | \$3,890 | 2.6% |
| Publishing including software | 636 | 0.4 |
| Motion picture and sound recording industries | 51 | 0.0 |
| Broadcasting and telecommunications | 2,615 | 1.7 |
| Information and data processing services | 588 | 0.4 |
| Finance and insurance | 7,506 | 4.9 |
| Federal Reserve banks, credit intermediation and related services | 3,281 | 2.2 |
| Securities, commodity contracts, investments | 894 | 0.6 |
| Insurance carriers and related activities | 3,306 | 2.2 |
| Funds, trusts, and other financial vehicles | 25 | 0.0 |
| Real estate and rental and leasing | 12,262 | 8.1 |
| Real estate | 11,168 | 7.3 |
| Rental and leasing services and lessors of intangible assets | 1,093 | 0.7 |
| Professional and technical services | 6,397 | 4.2 |
| Legal services | 1,371 | 0.9 |
| Computer systems design and related services | 941 | 0.6 |
| Other professional, scientific and technical services | 4,086 | 2.7 |
| Management of companies and enterprises | 2,261 | 1.5 |
| Administrative and waste services | 3,624 | 2.4 |
| Administrative and support services | 3,284 | 2.2 |
| Waste management and remediation services | 340 | 0.2 |
| Educational services | 882 | 0.6 |
| Health care and social assistance | 12,343 | 8.1 |
| Ambulatory health care services | 6,334 | 4.2 |
| Hospitals and nursing and residential care facilities | 5,193 | 3.4 |
| Social assistance | 816 | 0.5 |
| Arts, entertainment, and recreation | 897 | 0.6 |
| Performing arts, museums, and related activities | 413 | 0.3 |
| Amusement, gambling, and recreation | 484 | 0.3 |
| Accommodation and food services | 4,082 | 2.7 |
| Accommodation | 910 | 0.6 |
| Food services and drinking places | 3,172 | 2.1 |
| Other services, except government | 3,319 | 2.2 |
| Government | 23,182 | 15.2 |
| Federal civilian | 3,941 | 2.6 |
| Federal military | 4,434 | 2.9 |
| State and local | 14,807 | 9.7 |
| Total | \$152,099 | 100.0% |

Note: GDP values and percentages per industry may not add to statewide totals and totals for industry categories due to rounding.

Source: US. Bureau.

Chapter 2

Airport Administration and Finance

Administration

Approximately one-third of airports in the US are governed by independent airport authorities; one-third are governed by cities; and the remainder are governed by states, counties, regional authorities, or other entities (Transportation. *Innovative*).

Airports are mostly governed by independent airport authorities or cities. In Kentucky, one of the five commercial service airports is governed by a county airport boards, one by an urban county government board, two by regional airport authorities, and one by a city-county board.

The Cincinnati/Northern Kentucky airport is governed by a county airport board, the Lexington airport by an urban county government board, the Louisville and Paducah airports by regional airport authorities, and the Owensboro airport by a city-county board.

KRS Chapter 183 identifies the composition, purpose, and powers of local airport boards. Local boards establish the rates, charges, and fees for the use of the landing area, ramps, and other common aviation facilities.

Use Agreements

Airport-airline use agreements establish the rights, privileges, and obligations between an airport and its airline tenants.

Airport-airline use agreements establish the rights, privileges, and obligations between an airport and its airline tenants (Schulthess 11). These agreements vary and may be influenced by the size of the airport, the state of the airline industry, or the willingness of the airport's governing board to assume risk.

Among airlines, the trend is toward preferring shorter-term use agreements in order to give airlines the greatest amount of flexibility to adjust or eliminate service to airports if market conditions change. Airports may prefer longer-term agreements because their operations—namely terminals, runways, and other facilities—are fixed to that location (Transportation. *Airport*).

The two basic types of airport-airline use agreements are compensatory and residual. Airports typically incorporate elements of both types in their use agreements with airlines.

Under compensatory use agreements, airports have a high level of control over the financial operation of the airport but are subject to more financial risk. Airlines agree to pay certain fees and costs, but should an airport's operating revenues fall short of expenses, the

airport, not the airline, has to compensate for the difference (Schulthess).

Residual use agreements give airlines a higher level of control over the financial operation of the airport but also reduce the financial risk to airports. Airlines still pay landing, terminal, and other fees to the airport, but the airlines agree to pay for airport operating costs if they exceed operating revenues.

Use agreements can affect the amount of money an airport has available to provide economic incentives to airlines.

An airport's use agreement with its tenant airlines can affect its ability to provide economic incentives to airlines. Residual use agreements are generally more restrictive in this regard because they can give airlines considerable control over how an airport spends its revenues. All else equal, air carriers operating under this type of agreement will not want to support airport revenues being used to attract additional air carriers to the airport. The Cincinnati/Northern Kentucky airport's use agreement with its signatory airlines, for example, limits annual reserve funds to \$375,000 according to officials with that airport.

Restrictions on the Use of Airport Revenues

Federal law and policies restrict how airports receiving federal funds use airport revenues. Direct subsidies to air carriers by airport owners or operators are generally not allowed, but waiving fees or discounting landing or other fees for a limited promotional period are acceptable.

After the enactment of the Federal Aviation Administration Authorization Act of 1994, the Federal Aviation Administration (FAA) issued policies and procedures related to the generation and use of airport revenues (1999 Federal Register Vol. 64. No. 30).

Federal law prohibits airport owners or operators that receive federal financial assistance from using airport revenues for purposes other than those related to the airport (49 USC 47107(b) and 47133). Allowable uses include paying for capital and operating costs of the airport, local airport system, or other local facilities directly related to the airport. Certain indirect costs may also be allocated to airports but must be related to the operation of the airport.

Direct subsidies to air carriers by airport owners or operators are generally not allowed, but waiving fees or discounting landing or other fees for a limited promotional period are acceptable. The FAA does not provide specific rules but generally accepts programs that last 1 year or less. These types of direct subsidies must be offered to all users of the airport and provided to all users that are willing to meet the requirements established by the airport for receipt of the subsidy. Advertising or marketing for airlines as

identified under the Permitted Activities section are also acceptable.

Permitted uses of airport revenue, each of which must be related to the airport, airport system, or the delivery of local air transportation service, include

- capital or operating costs;
- activities that promote competition, public and industry awareness, new air service and competition, and expenses for personnel that promote air service;
- promotional expenses designed to increase air travel;
- reimbursement to airport owners or sponsors for capital and operating costs;
- lobbying and attorney fees;
- government costs such as travel costs to meet FAA officials;
- related general costs of government;
- community activities and events; and
- capital or operating costs of related ground access projects such as rail terminals.

Prohibited uses of airport revenue include

- direct or indirect payments that exceed the value of services provided to the airport;
- inconsistently applied direct or indirect payments;
- general economic development;
- marketing and promotional activities not related to the airport;
- payments in lieu of taxes that exceed fair and reasonable values;
- payments to nonsponsoring governmental bodies for lost tax revenues;
- loans or investments in state or local agency at less than the prevailing rate of interest;
- land rental or use for nonaeronautical purposes at less than the fair rental or market value;
- rent-free or nominal-fee use of land by sponsor for certain nonaeronautical purposes;
- governmental impact fees that exceed value of services or facilities provided; and
- community events or activities unrelated to the airport (49 USC 40117 and 14 CFR Part 158).

Sources of Revenue

Many airport revenues are associated with the transportation of passengers and cargo. Airlines and passengers pay fees for using an airport's facilities, travelers pay to park their cars at an airport, and rental car companies and concessionaires pay fees to airports to operate businesses on site.

Proceeds from bonds issued by airports or other governmental authorities are typically used to fund long-term capital projects such as expanding runways or remodeling terminal buildings.

Grants and loans from federal, state, and local governments are another source of revenue. Federal government grants represent a significant source of funds for many airports and are commonly required to be used to pay for capital improvements at an airport.

Airports may also receive revenue from ancillary operations. For example, an airport may own an adjacent industrial park or farmland and receive regular rent payments for the use of that land. Airports may also receive revenue from fixed-base operators—companies that operate aircraft solely at the airport.

Operating Revenues

Aeronautical revenues are related to flying passengers and include landing fees and terminal fees. Nonaeronautical revenues, such as from parking or ground transportation, are generally unrelated to air transportation.

These revenues, derived from activities directly related to the operation of an airport, can be broadly categorized as passenger aeronautical, nonpassenger aeronautical, and nonaeronautical.

Passenger aeronautical revenues are related to flying passengers and include landing fees and terminal fees. Nonpassenger aeronautical revenues come from activities that are indirectly related to the transportation of passengers and cargo and include such items as aviation fuel taxes and hangar rental fees. Nonaeronautical revenues are generally unrelated to air transportation and include, for example, parking and ground transportation revenues.

Nationally, aeronautical activities comprise approximately two-thirds of operating revenues for large-hub airports, one-half for medium hubs and nonhubs, and less than one-half for small hubs.

Large-hub airports, on average, receive a higher proportion of operating revenues from aeronautical activities than do medium and small hubs and nonhubs. In 2009, aeronautical activities accounted for almost two-thirds of operating revenues for large-hub airports, approximately one-half of revenues for medium hubs and nonhubs, and less than one-half of revenues for small-hub airports.

Aeronautical operating revenues were proportionally greater for 999 large-hub airports due, in part, to a greater reliance on terminal fees. Large-hub airports earned, on average, one-third of their operating revenues from terminal fees, compared to one-ninth for small hubs. Terminal fees include rents paid by airlines for accessing and using facilities provided by an airport. As a result, airports with higher volumes of passenger and cargo transportation earned greater amounts of revenue compared with airports that had lower traffic volumes.

Parking and ground transportation generate significant revenue for airports. Medium- and small-hub airports rely on these revenue sources more than do large-hub airports.

For revenues derived from nonaeronautical services, medium- and small-hub airports earned, on average, proportionally more than large-hub airports. Parking and ground transportation revenues were important reasons. Medium- and small-hub airports received, on average, nearly 25 percent of their operating revenues from parking and ground transportation in 2009; large-hub airports received approximately 15 percent; and nonhubs received approximately 12 percent.

Table 2.1 identifies the distribution of operating revenues for Kentucky's four primary airports in 2009. For this table and some others in this chapter, Owensboro-Daviess County Airport is not included because it was a general aviation airport until recently and was not required to submit financial data to the Federal Aviation Administration.

Table 2.1
Operating Revenues Per Airport
2009

| Revenue Category | | Cincinnati/ Northern Kentucky | Louisville | Lexington | Paducah |
|------------------|-----------------------------------|-------------------------------------|------------|-----------|---------|
| | | Aeronautical | Passenger | 46.7% | 50.8% |
| | Nonpassenger | 9.0 | 4.8 | 3.0 | 34.0 |
| | Subtotal | 55.7% | 55.6% | 40.3% | 50.6% |
| Nonaeronautical | Parking and ground transportation | 22.4 | 23.8 | 31.6 | 14.5 |
| | Rental cars | 7.3 | 12.1 | 18.2 | 28.7 |
| | Other | 14.7 | 8.4 | 9.9 | 6.2 |
| | Subtotal | 44.4% | 44.3% | 59.7% | 49.4% |
| Total | (percent) | 100.0% | 100.0% | 100.0% | 100.0% |
| | (in millions of \$) | \$82.8 | \$58.7 | \$11.9 | \$0.9 |

Note: Percentages may not add to subtotal and total percentages due to rounding.
 Source: Program Review staff analysis of US. Federal. Compliance.

In 2009, aeronautical activities made up more than 55 percent of operating revenues at the Cincinnati/Northern Kentucky and Louisville airports. Just more than one-half of operating revenues at the Paducah airport came from aeronautical activities; 40 percent of the Lexington airport's revenues did so.

Consistent with national averages, the percentage of aeronautical operating revenues for Kentucky airports varied by the size of the airport. The Louisville and Northern Kentucky airports received proportionally higher amounts of revenues from passenger airline landing fees and terminal fees than either the Lexington or Paducah airport.

At each airport, most nonaeronautical revenues came from parking and ground transportation and rental cars. As a percentage of total operating revenues, these sources accounted for 30 percent to 50 percent of total airport operating revenues.

Relative to airports nationally, the Lexington and Paducah airports received a greater proportion of revenues from parking and ground transportation; the Northern Kentucky and Louisville airports received slightly less. As a proportion of the total, operating revenues collected from rental car companies were considerably higher at the Paducah airport. According to officials from that airport, this is likely attributable to the large geographic area the airport serves, which means that more people will require rental cars.

Bonds

Governmental entities that operate or support airports commonly issue bonds to pay for long-term capital projects. According to an estimate by Council International-North America, approximately 30 percent, or \$28 billion, of all capital projects from 2009 to 2013 will be funded by bonds (Transportation. *Airport* 8-9).

State Government

Jet fuel taxes help fund a state aviation economic development fund. The Kentucky Department of Aviation also has authority to issue up to \$60 million in bonds for the purpose of improving airports in Kentucky.

An aviation economic development fund in Kentucky provides for the development, rehabilitation, and maintenance of publicly owned or operated aviation facilities (KRS 183.525). Sales and use taxes collected on jet fuel, state appropriations, gifts, grants, and federal funds can be deposited into this fund.

The Kentucky Department of Aviation also has authority to issue up to \$60 million in bonds for the purpose of improving airports in Kentucky. According to LRC staff, only \$9 million has been used to date.

Federal Government

The federal government provides the largest amount of funding.

The federal government provides the largest amount of funding to airports.

The federal Airport Improvement Program provides funds to airports that can be used to help pay for planning and capital projects. Since FY 2005, Kentucky's five commercial airports have received \$284.7 million through the program.

Airport Improvement Program. The Airport Improvement Program (AIP) provides funds to airports that can be used to help pay for planning and capital projects such as runway improvements. The program is funded through user fees, fuel taxes, and other sources.

AIP funds a portion of a project's total costs. Up to 75 percent of eligible project costs for large and medium primary hub airports can be funded by AIP allocations; the remainder must come from the airport or other sources. Up to 95 percent of eligible projects for small and general aviation airports can be funded by AIP. For all Kentucky airports except Cincinnati/Northern Kentucky, Louisville, and Lexington, the state and the airport authority each pays 2.5 percent of the 5 percent nonfederal contribution.

Table 2.2 lists the amount of AIP funding the five primary airports in Kentucky received from FY 2005 to FY 2009.

Table 2.2
Airport Improvement Program Funding Per Airport (in millions of dollars)
Fiscal Year 2005 to Fiscal Year 2009

| Airport | Fiscal Year | | | | | Total |
|------------------------------|---------------|---------------|---------------|---------------|---------------|----------------|
| | 2005 | 2006 | 2007 | 2008 | 2009 | |
| Cincinnati/Northern Kentucky | \$28.3 | \$31.0 | \$37.3 | \$23.1 | \$11.5 | \$131.2 |
| Louisville | 32.0 | 19.4 | 21.3 | 14.3 | 6.8 | 93.8 |
| Lexington | 9.1 | 10.0 | 3.5 | 8.9 | 9.6 | 41.1 |
| Paducah | 4.4 | 1.2 | 0.8 | 1.1 | 1.0 | 8.6 |
| Owensboro | 2.5 | 3.1 | 1.2 | 0.4 | 3.2 | 10.0 |
| Total | \$76.3 | \$64.7 | \$64.1 | \$47.5 | \$32.2 | \$284.7 |

Note: Entries may not add to totals as shown for fiscal years and airports due to rounding.
 Source: US. Federal. "FAA."

The federal Essential Air Service program subsidizes commuter air service to small communities. Owensboro and Paducah receive funding from the program.

Essential Air Service Program. The federal Airline Deregulation Act in 1978 gave airlines the ability to determine, to a large extent, which domestic markets to serve and the price of fares to charge. The federal government established the Essential Air Service (EAS) program to help smaller communities maintain air service. Under the program, subsidies are given to commuter airlines that provide service to smaller communities.

As of May 2010, 154 communities in the US, nearly one-third of which were in Alaska, were recipients of subsidized commuter air service under the EAS program. Total subsidies were \$175 million (US. Dept. Office. *U.S.*).

Owensboro and Paducah currently receive subsidized commuter air service under the EAS program. For Owensboro, the subsidy amount is almost \$1.1 million through August 31, 2011. Pacific Wings Airlines provides the commuter service. For Paducah, the subsidy amount is almost \$570,000 through December 31, 2011. SkyWest Airlines provides commuter service (US. Dept. Office. *U.S.*)

The federal Small Community Air Service Development Program helps smaller communities enhance their air service by providing grants that can be used to pay for advertising, promotional activities, studies, or financial incentives to airlines.

Small Community Air Service Development Program. The Small Community Air Service Development Program (SCASDP) is designed to help smaller communities enhance their air service. Only communities that had small-hub airports or smaller as of 1997 and had insufficient air carrier service or unreasonably high airfares as of 1997 are eligible. Up to 40 communities receive grants each year. Over the past 3 years, grants have ranged from \$20,000 to nearly \$1.6 million (US. Dept. Office. Small).

SCASDP grants can be used to pay for advertising or promotional activities that improve air service to the community and to pay for financial incentives, including subsidies or revenue guarantees to air carriers and ground service providers. Studies that measure air service deficiencies and the employment of air service development staff may also be funded (US. Dept. Office. Small). Improvements to air transportation service are expected to continue after the initial grant expenditures have ended.

In Kentucky, seven communities have received Small Community Air Service Development Program grants from 2002 to 2009. The Lexington airport used a \$600,000 grant to provide incentives to an airline for new air service.

As shown in Table 2.3, seven communities in Kentucky have received SCASDP grants totaling \$3.6 million since FY 2002. According to officials from the Lexington airport, the grant it received in FY 2007 was used to help fund a revenue guarantee for new air service by AirTran Airways.

Table 2.3
Kentucky Community Recipients of Small
Community Air Service Development Program Grants
Fiscal Year 2002 to Fiscal Year 2009

| Fiscal Year | Community | Grant |
|--------------------|------------------|--------------------|
| 2002 | Paducah | \$304,000 |
| 2002 | Somerset | 95,000 |
| 2003 | Owensboro | 500,000 |
| 2005 | Somerset | 950,000 |
| 2006 | Big Sandy | 90,000 |
| 2007 | Bowling Green | 150,000 |
| 2007 | Greenville | 450,000 |
| 2007 | Lexington | 600,000 |
| 2009 | Bowling Green | 500,000 |
| Total | | \$3,639,000 |

Source: US. Dept. Office. Small.

Passenger Facility Charges

Airports may charge passengers for the use of their facilities. Under federal guidelines, airports controlled by public agencies may collect up to \$4.50 per passenger per enplanement. Airports may use the proceeds, with FAA approval, to pay for projects that improve airport safety, security, or capacity; reduce noise; or increase air carrier competition (US. Federal. Passenger).

Since 1990, passenger facility charges have been estimated to fund at least 30 percent of airport capital improvement projects. These proceeds have helped pay to construct new runways, improve or expand terminal projects, and pay interest on airport bonds. Passenger facility charges have also been used to build gates in order to increase airline competition and lower airfares at airports (Airports).

In 2009, the Cincinnati/Northern Kentucky airport collected \$16.1 million in passenger facility charges, Louisville collected \$4.6 million, Lexington collected \$1.9 million, and Paducah collected \$50,000. The passenger facility charge was \$3 per enplanement at the Northern Kentucky, Louisville, and Paducah airports and \$4.50 at the Lexington airport.

Operating Expenses

Personnel and contracting service expenses for the Cincinnati/Northern Kentucky, Louisville, and Paducah airports were each about 38 percent of total operating expenses. The corresponding percentage for the Lexington airport was 46 percent.

Personnel-related expenses, which include payments to employees and contractors, was the largest category of operating expenses for US airports in 2009. As a percentage of total operating expenses, these costs were similar among different size categories of airports.

Table 2.4 identifies personnel-related expenses as a percentage of total operating expenses at Kentucky's primary airports. For three of the four primary airports, these expenses were comparatively smaller than at airports nationally. Personnel and contracting service expenses for the Northern Kentucky, Louisville, and Paducah airports were each about 38 percent, which was 5 to 10 percentage points lower than at airports of similar hub size. As a percentage of total operating expenses, personnel and contractual service expenses at the Lexington airport were nearly identical to the national figure for small-hub airports.

Table 2.4
Operating Expenses Per Airport
2009

| Operating Expense | | Cincinnati/ Northern Kentucky | Louisville | Lexington | Paducah |
|--------------------------|----------------------|--|-------------------|------------------|----------------|
| Personnel-related | Personnel | 27.4% | 24.1% | 36.4% | 32.2% |
| | Contractual services | 10.7 | 13.5 | 9.7 | 5.4 |
| | Subtotal | 38.1 | 37.6 | 46.0 | 37.7 |
| All Other Expenses | | 61.9 | 62.4 | 54.0 | 62.3 |
| Total | | 100.0% | 100.0% | 100.0% | 100.0% |
| (in millions of \$) | | \$40.7 | \$19.1 | \$8.2 | \$0.8 |

Note: Percentages may not add to subtotal and total percentages due to rounding.

Source: Program Review staff analysis of US. Federal. Compliance.

Chapter 3

Incentives for Provision of Air Service

Specific statistics on how often flights are added with and without incentives are unavailable. It is perceived by many that incentives to airlines as an inducement to increase or maintain air service have become more frequent over time.

Airlines add new flights frequently. A quick Google search resulted in announcements made in 2010 for 76 new planned flights originating at 10 airports across the country (Ahles; “Alaska”; “Allegiant”; “American Airlines Partners”; “American Airlines to add”; “American Eagle”; “American to add”; “Delta airlines adding”; “Delta Airlines to Add”; Mutzabaugh). For some unknown share of flights added in recent years, incentives were provided to airlines to increase or, in some cases, just maintain, air service. It is perceived by many that incentives to airlines as an inducement to increase or maintain air service have become more frequent over time, but specific statistics on how often flights are added with and without incentives are unavailable.

As with other economic development projects, it is often unknown whether a particular increase in air service would have been provided even if an incentive were not offered. As an illustration, a bill in the 2010 South Carolina General Assembly would have created a \$15 million fund for airline incentives, widely perceived as an effort to lure Southwest Airlines to begin service to the state. The bill passed the House handily. There was more opposition in the Senate, but while the bill was still under consideration by that chamber, Southwest announced that it would begin service from two South Carolina cities in 2011 whether the bill was enacted or not. If the bill had been enacted and Southwest had taken the incentive money, it would have been reasonable to assume that the incentive was necessary, and that would have been the story. As reported in the local media, now the story—literally—is that there was an especially good marketing effort directed to Southwest: “How Charleston landed Southwest Airlines: There was a lot of wooing, but there were no economic incentives” (Bird). The “wooing” of Southwest might have been critical, but it is also possible that Southwest made a decision based strictly on the potential market for air service in South Carolina. The airline may end up taking incentives provided by the airports and other local entities, so it is not even necessarily the case that incentives did not matter. The point is that establishing cause and effect for incentives for air service is, at best, complicated.

The first section of this chapter describes the more common techniques that airports and other entities have offered to increase or maintain service. The second section summarizes specific

examples of incentives that airports, private entities, and local governments have offered.

The third section summarizes incentives for air service that have been provided by five states. These are intended as examples only. The actual number of incentives that have been provided by state governments is unknown, but it appears that state incentives are uncommon. Even rarer are state incentive programs that provide statutory guidelines and a pool of state funding for incentives over time. The only two such programs in operation that Program Review staff were able to identify are covered in the last section of the chapter, along with two proposed state programs.

Air Service Development Techniques

Among the methods that have been used in an effort to increase air service or maintain existing service is the minimum revenue guarantee, which establishes a minimum level of revenue that a carrier will get for a route. The airport or other entity making the guarantee is responsible for making up the shortfall if revenue from passengers is less than the guaranteed amount.

Passenger Air Service Development Techniques, a 2009 report from the Transportation Research Board, identifies methods that have been used in an effort to increase air service or maintain existing service. For the report, 41 relatively small airports were surveyed on their use of the techniques.

A minimum revenue guarantee establishes a minimum level of revenue that an airline will get for specified service to a specified destination for a specified amount of time. If revenue from passengers on the guaranteed flights is less than the agreed-upon minimum, then the airport or other entity making the guarantee is responsible for making up the shortfall. Depending on revenue from passengers, the airport or other entity may end up paying all, part, or none of the guarantee (104-105). More than one-half of the surveyed small airports reported using revenue guarantees (11).

In a guaranteed ticket purchase program, businesses or individuals deposit funds in a bank account to be used for purchasing tickets on a specified airline over a specified period.

In a guaranteed ticket purchase program, also called a travel bank, businesses or individuals deposit funds in a bank account to be used for purchasing tickets on a specified airline over a specified time period. Such a program is an indicator of commitment from the community, particularly business customers (106). Less than 20 percent of the surveyed airports reported using guaranteed ticket purchases (11).

Cost subsidies are financial incentives to reduce an airline's costs for providing a specified service. Common examples are waivers or reductions in landing fees or terminal rent for a specified period.

Cost subsidies are financial incentives to reduce an airline's costs for providing a specified service. Common examples are waivers or reductions in landing fees or terminal rent for a specified period. Airports may also provide, for a fee, ground services that an airline would otherwise have to provide itself. This category also includes cash subsidies that are not contingent on the airline earning a

specified amount of revenue for the service being provided (107-108). Approximately 60 percent of the airports surveyed indicated that they used some form of cost subsidy (11).

Marketing or advertising for an air service, provided or purchased by the airport or other entity, is the most common incentive.

According to the survey done for the Transportation Research Board report, more than 80 percent of the small airports surveyed indicated that they engaged in marketing of an air service, making it the most commonly used technique (11). Marketing or advertising for an air service is provided or purchased by the airport or other entity (109).

Examples of Incentives Offered by Airports, Local Governments, and Private Entities

Comprehensive data on how often incentives for air service have been provided are unavailable. The report gives examples of incentives that have been offered by airports, local governments, and private entities to increase service to domestic and international destinations. In some of the examples, the incentive was successful in that the air service was maintained after the incentives ended. In other cases, the service was not maintained.

Because all the incentives that have been offered by airports, private entities, or local governments cannot be determined, the cases summarized below are intended as examples, which may not be representative of all incentives. The examples include different sources of incentives: airports, local governments, private entities, or some combination. Some of the sample incentives are to increase service to domestic destinations; some are for international service. Some of the sample incentives are revenue subsidies; some reduce airlines' costs by reducing or waiving landing fees for a period of time or having the airport provide services traditionally provided by airlines. In some of the examples, the incentive was successful in that the air service was maintained after the incentives ended. In other cases, the service was not maintained.

In 2010, the Phoenix, Arizona, city council authorized Phoenix Sky Harbor International Airport to offer financial incentives of up to \$900,000, subject to council approval, to help an airline adding an international flight. Most of the funding would be used for marketing (Geresma).

In 2008, Frontier Airlines received an incentive through an existing \$1 million fund created by the Baton Rouge Metro Council in Louisiana. The airline operated a flight from Baton Rouge Airport to Denver, Colorado. The airline, which went bankrupt that year, used \$577,000 in incentives before abandoning the route (Jacobs).

In 2004, AirTran Airways began service to Atlanta, Georgia, and Baltimore/Washington International Airport in Maryland from Sarasota Bradenton International Airport in Florida. Sarasota Bradenton was able to provide incentives after receiving a

\$1.5 million federal Small Community Air Service Development Grant (“AirTran”). At the time of this report, AirTran was still flying daily nonstop flights to Atlanta and Baltimore/Washington and had added service to Boston, Massachusetts; Chicago, Illinois; Indianapolis, Indiana; and Milwaukee, Wisconsin.

In 2009, the airport, local government, and private entities proposed a package of incentives worth approximately \$10 million to woo Southwest Airlines to offer flights at the Pensacola Gulf Coast Regional Airport in Florida. The area Chamber of Commerce organized a campaign to have local residents pledge to buy Southwest tickets. The airport would waive landing fees and airport rent for 2 years. The county would increase its lodging tax to generate \$3 million to be offered as a subsidy to Southwest. More than 45,000 nights of lodging at hotels and condominiums would be donated to Southwest for its use in vacation packages (Lyman). At the time of this report, Southwest does not offer service at the Pensacola airport and has not announced plans to do so.

As part of its agreement in 2010 with American Airlines to get daily flights from the airline’s American Eagle affiliate to Dallas, Texas, the Augusta Regional Airport in Georgia agreed to run American Eagle’s ticket counter for the first year and handle ramp services. The estimated cost of providing these services for the year is \$105,000. The airport is also waiving landing and terminal rental fees for the first year (Zureick).

In July 2009, Oregon’s Portland International Airport and the City of Portland agreed to provide \$3.5 million to encourage Delta Air Lines to maintain its nonstop flight to Tokyo, Japan, after Deutsche Lufthansa ended flights to Frankfurt, Germany, from Portland. In 2010, Delta agreed to maintain the Tokyo service and nonstop service to Amsterdam, Netherlands, without the subsidy (Read).

In 2008, Lufthansa stopped providing nonstop service to Munich, Germany, from Denver International Airport after an agreement for subsidized service for 1 year expired. The airport had provided reduced landing fees and marketing worth \$2 million, with a contribution from the Metro Denver Economic Development Corporation (Leib).

Other airports that have been reported as offering incentives include those in Austin, Texas; Columbus, Georgia; Dallas-Fort Worth, Texas; Detroit, Michigan; Manchester, New Hampshire; Medford, Oregon; Miami, Florida; New Orleans, Louisiana; and

Providence, Rhode Island. As an especially detailed example, Appendix B contains information about its incentive programs that California's Mineta San José International Airport posts on its website.

Ground Services

Ground services include ramp services such as towing aircraft, on-ramp services such as fueling and deicing, on-board services such as cleaning the cabin, operation of ramp equipment such as steps for passengers, and in-terminal services such as checking in passengers. An airline typically handles these services itself or contracts for them with an agent or another airline. Some airports, mostly small- and medium-sized commercial or general aviation, have assumed responsibility for providing all or some ground services.

Ground services include ramp services such as towing aircraft, on-ramp services such as fueling and deicing, on-board services such as cleaning the cabin, operation of ramp equipment such as steps for passengers, and in-terminal services such as checking in passengers. An airline typically handles these services itself or contracts for them with an agent or another airline. Some airports, mostly small- and medium-sized commercial or general aviation, have assumed responsibility for providing all or some ground services. In some cases, airports have taken over ground services to make money or because the agent providing such services at the airport left the market. Another purpose has been to entice an airline to begin or maintain service at the airport (*Transportation. Airport*).

Mobile Station Services Program. The Station Services program at Alabama's Mobile Regional Airport is an example of an airport providing ground services. In 2001, United Express provided ground services for its own flights to Chicago and Washington, DC, and also for US Airways Express flights to Charlotte, North Carolina. When United announced that it would be leaving the Mobile, Alabama, market, the airport decided to begin offering ground services to avoid losing US Airways Express flights too (Bordes).

The Mobile Station Services program provides ground services for any carrier that wishes to use the service. The airport used a \$450,000 federal Small Community Air Service Development Program grant to set up the program, which included purchasing equipment and hiring and training staff. Carriers pay a per-turn fee and terminal rent for the use of ticket counters, gate areas, and baggage carousels. US Airways Express has used the program's services since it began in 2001. American Eagle used the program when it began service to Mobile in 2005 but began operating its own ground handling services in 2008 as its operations at the airport expanded (Bordes).

Examples of Incentives Offered by State Governments

The cases summarized below cover incentives for air service that have been provided in seven specific instances in five states: Pennsylvania, Utah, Florida, Ohio, and North Carolina. The examples include incentives for adding domestic and international flights and for expanding specific airlines' capacity at airports. The incentives offered by state government ranged in value from \$650,000 to more than \$16 million.

This is not an exhaustive list. It is unknown how many incentives have been provided by state governments, so these examples may not be representative. Based on the number of incentives for which information can be found in publicly available sources, it appears that state incentives are uncommon.

Incentives for International Service

Examples are described of incentives for air service that have been provided by five states: Pennsylvania, Utah, Florida, Ohio, and North Carolina. The examples include incentives for adding domestic and international flights and for expanding specific airlines' capacity at airports. The incentives offered by state government ranged in value from \$650,000 to more than \$16 million. This is not an exhaustive list; it is unknown how many incentives have been provided by state governments. Based on the number of incentives for which information can be found in publicly available sources, it appears that state incentives are uncommon.

In terms of simply whether flights continue to be offered, the results for state incentives for international flights are mixed. In three instances noted below, the incentives were provided to subsidize nonstop international service for a start-up period. One of the flights is still being provided; another is operating on a reduced schedule. It is unclear whether the third flight will continue once its period of subsidized operations ends.

Pennsylvania. In June 2009, Delta Air Lines began nonstop flights to Paris, France, from Pittsburgh International Airport, the first transatlantic flight for the airport since 2004. The private Allegheny Conference on Community Development and the office of the governor pledged up to \$9 million over 2 years in revenue guarantees. Each would contribute up to \$2.5 million in the first year and up to \$2 million in the second year of the agreement (Belko. "Delta's"). The airport is spending \$600,000 over the 2-year period to market the flight ("Pittsburgh").

In addition to the financial support, the Allegheny Conference on Community Development recommends that leaders of member organizations require that their employees traveling to Europe on business use the Delta flight unless there is compelling justification not to do so (Belko. "Nonstop").

In terms of simply whether flights continue to be offered, the results for state incentives for international flights are mixed. In three instances noted here, the incentives were provided to subsidize nonstop international service for a start-up period. One of the flights is still being provided; another is operating on a reduced schedule. It is unclear whether the third flight will continue once its period of subsidized operations ends.

Expectations were high before the flights began, and local leaders said that they did not expect to have to spend the \$9 million in incentives. The chair of the airport authority analogized the subsidies to “life insurance on a healthy 20-year-old. You’re probably not going to have to pay off” (Pfister). However, within the first year of the flights, the Allegheny Conference on Community Development issued a report anticipating that the conference and the state would have to pay the maximum \$5 million total to make up for missed revenue targets for the first year of the agreement. Both could have to pay the full \$4 million for the second year unless revenues improve (Belko. “Delta’s”).

Utah. Delta began a nonstop flight to Paris, France, from Salt Lake City International Airport in June 2008, the first transatlantic flight from the airport. The airport and state provided \$1.85 million in incentives. The airport provided \$655,000 cash and \$345,000 in waived landing fees. The state incentives were a \$250,000 grant from the Governor’s Office of Economic Development and in-kind marketing by the Office of Tourism worth \$600,000. In the 2 years preceding the initiation of the flight to Paris, Salt Lake City was Delta’s fastest-growing hub; passenger traffic was up by 40 percent, with 30 new destinations and 50 new flights added (Loftin). As of September 2010, the flight to Paris was still in operation.

In June 2009, Delta added a flight from Salt Lake City to Tokyo, Japan. The state incentives were a \$250,000 grant from the Governor’s Office of Economic Development and \$400,000 in marketing by the Office of Tourism. The airport allocated an additional \$100,000 for airport security personnel (Hancock. “Delta begins”; State of Utah. Governor’s. “Minutes” and “News”). The Tokyo flights were initially scheduled for 5 days per week. Within a month, Delta announced that flights would be reduced to 4 days per week. Later, flights were suspended from October 1, 2009, to May 14, 2010 (Hancock. “Delta to suspend”). The flights were resumed on a seasonal basis in May 2010.

Incentives for Domestic Service

Results for state incentives for domestic service are also mixed. In some instances, flights have been dropped by airlines during the subsidized period. State, local, and airport incentives were provided to increase Continental Airlines' capacity at the Cleveland, Ohio, airport. After Continental's merger with United Airlines, there is now an agreement to limit reductions in capacity at Cleveland by the merged airline. Two states provided incentives to Skybus Airlines, which has since gone bankrupt.

The results for incentives for domestic service are also mixed. In some instances, flights have dropped during the subsidized period. State, local, and airport incentives were provided to increase Continental Airlines' capacity at the Cleveland, Ohio, airport. While the goals of the incentives agreement are unlikely to be met given Continental's merger with United Airlines, there is an agreement to at least limit reductions in capacity at Cleveland by the merged airline. The final example is Skybus Airlines, which was granted incentive packages by two state governments before it went bankrupt.

Florida. In 2009, Delta Air Lines received a \$1.5 million revenue guarantee from the state and local governments to add flights beginning April 1 between Tallahassee and Tampa, Orlando, and Fort Lauderdale. The state's commitment was \$750,000. Leon County's and Tallahassee's shares were \$375,000 each. According to the agreement, if Delta's passenger revenue from the flights is less than the projected \$11.5 million needed to operate the flights for 1 year, then the governments will make up the difference up to \$1.5 million. (Jackovics. "Taxpayers"). Within 6 months, only the between Tallahassee and Fort Lauderdale was still being offered (Jackovics. "Delta").

Ohio: Continental Airlines. Cleveland Hopkins International Airport's situation has changed from plans in 2007 for significantly increased domestic and international service to a legal agreement to limit reductions in service.

In 2007, Ohio state government offered incentives of more than \$16 million for Continental Airlines to expand its capacity at the Cleveland airport. According to a joint press release from the State of Ohio, the City of Cleveland, and Continental, the airline was to initially offer 50 more flights and add 20 new nonstop destinations by the summer of 2008. Nonstop seasonal service to Paris, France, was to begin in May 2008. By early 2009, Continental was to have added more than 12 additional flights, principally on mainline aircraft (City of Cleveland).

As of September 2007, Continental had been awarded a \$900,000 Ohio Rapid Outreach Grant, a 10-year Ohio Job Creation Tax Credit worth \$9.1 million, and a \$550,000 Ohio Investment in Training Grant (City of Cleveland; Huddle). Among the provisions of the tax credit were that 711 full-time jobs would be created and that Continental would maintain operations at the airport for 20 years ("Continental"). Continental also was to receive employment

pre-screening, testing, and recruitment services through the Ohio Department of Job and Family Services (City of Cleveland).

As of May 2008, 7 of the 20 new planned flights had been postponed and only about 200 jobs had been created. None of the \$16 million from the state had been used by Continental (Roguski). The nonstop flight to Paris was not resumed in 2009 (Kroll). The airport's flight to London, England, its remaining transatlantic nonstop, was not resumed in 2010 (Grant).

In May 2010, the boards of United Airlines and Continental agreed to a merger that would create the largest airline. At the time of this report, the merger has been approved by the stockholders of both companies, the US Department of Justice, and the Ohio Attorney General (Shannon). The approval by the Ohio attorney general came after the office reached an agreement with United Airlines and Continental Airlines to maintain "specified levels of air service." The airlines agreed to remain committed to the airport for at least 5 years. In the first 2 years, the merged airline is to maintain no less than 90 percent of the two airlines' average daily departures in the year before the merger's closing date. Under specified conditions, the merged airline can reduce its commitment after the first 2 years. For example, if the profits of the merged airline for Cleveland flights are sufficiently low or losses sufficiently high, the commitment to a minimum number of departures can be reduced or eliminated (Karp).

Ohio: Skybus Airlines. In 2006, the State of Ohio, the City of Columbus, and the Port Columbus International Airport initiated an incentive package of \$57 million to base Skybus Airlines at the airport. Skybus was a start-up discount airline with significant local investment (Rose. "Skybus' planned").

State government proposed an incentive package valued at approximately \$16 million. The bulk of the package was a \$7.7 million tax credit for job creation and a \$5 million grant for infrastructure improvement. The remaining incentives were a loan to purchase machinery and equipment and funding for screening, testing, and training of employees. (State of Ohio. Dept. Press. "Development"; "Job"; "Johnson"). The Columbus city council approved incentives worth \$14 million consisting of tax credits, grants, loans, and performance incentives (Winn). The airport offered \$4 million in incentives through its Airline Incentive Program for new and existing airlines that add service. The enhancements to terminal capacity needed to support the increase in passengers anticipated would cost up to \$23 million (Columbus).

Skybus Airlines had sold 200,000 tickets before service began at Port Columbus (Rose. “Skybus up”). Within its first month of operation, the airline was adding new destinations across the country (Rose. “New cities”). By early 2008, Skybus was still adding destinations, but it was also dropping them and had nearly abandoned the west coast market (Rose. “Skybus trims”). Less than 1 year after service was initiated at Port Columbus, the airline shut down abruptly in April 2008 and went bankrupt, stranding passengers at airports across the country (Johnson). Only a small share of the \$57 million in state and local incentives was actually paid out. The airline estimated that it would pay 76 cents on the dollar to general unsecured creditors such as the state Department of Development and the airport authority. As part of Skybus’s bankruptcy, the Department of Development filed a claim for the return of \$1.15 million in grant money. The airport authority’s claim was for \$5.2 million (Rose. “Skybus shareholders”).

North Carolina. In 2007, Skybus Airlines was offered more than \$13 million of incentives by North Carolina state government, local governments, Piedmont Triad International Airport, and local private organizations to make Greensboro its second base city. According to the airline, this would result in the creation of 375 jobs with the airline and a \$350 million investment in the Greensboro/Winston-Salem area. The governor’s office estimated that more than \$9 million in new state tax revenue would be created (“Skybus”). Offering tickets for as low as \$10, Skybus expanded service at the airport in early 2008 and had 18 daily flights at its peak. As noted above, the airline went bankrupt in 2008.

State government’s contribution to the incentives was a \$3.98 million Job Development Investment Grant from the Department of Commerce. Local governments and organizations pledged approximately \$1.5 million for marketing. The airport’s incentives totaled approximately \$8.6 million: \$6.3 million for construction and updating of facilities, \$300,000 for marketing, and \$2 million or more through a program that pays a fee for each passenger boarding new nonstop flights (Barron). Because many of the incentives were contingent on performance and Skybus remained in business so briefly, only a small percentage of the incentive funding was spent. In 2010, airport officials estimated that \$1 million had been spent (Johnson).

State Incentive Programs in Operation

Program Review staff identified two state incentive programs that are being offered in Kansas and Wyoming, and two more that were proposed in a state legislature but not enacted in Louisiana and South Carolina. In each case, the incentive is in the form of an ongoing fund that can be used to fund multiple projects.

Program Review staff identified two state incentive programs that are being offered in Kansas and Wyoming, and two more that were recently proposed but not enacted in the South Carolina and Louisiana legislatures. In each case, the incentive is in the form of an ongoing fund that can be used to fund multiple projects. Appendix C contains the statutory language for the Kansas and Wyoming programs. Appendix D contains the bills that would have created the South Carolina and Louisiana programs.

Kansas

Wichita city leaders and the Regional Economic Area Partnership, comprising city and county governments in south central Kansas, began working with area businesses in 2001 to create a travel bank program. The goal was to attract low-cost carriers to Wichita's Mid-Continent Airport ("City, area"). The low-cost carrier AirTran Airways began service in 2002, also benefiting from incentives made possible by initial funding of more than \$3 million from the City of Wichita. As of FY 2006, Wichita had funded more than \$8 million in incentives; Sedgwick County had funded \$1 million (Harrah).

In 2006, the Kansas state legislature established the Affordable Airfare Fund. The goals for the fund include providing more flight options, more competition for air travel, and affordable airfares. From FY 2007 to FY 2011, the total state appropriation for the program was nearly \$25 million. Local contributions totaled more than \$8.2 million over this period. Almost all the incentive money has gone to AirTran Airways as revenue guarantees to provide daily round-trip service to Atlanta, Georgia, from Wichita.

In 2006, the state legislature established the Affordable Airfare Fund. The goals for the fund included providing more flight options, more competition for air travel, and affordable airfares. A \$5 million fund was created with expenditures to be made in annual grants to the Regional Economic Area Partnership through appropriations acts of the legislature. Each grant must be matched by a 25 percent contribution from local government or private entities. From FY 2007 to FY 2011, the total state appropriation was nearly \$25 million.¹ Local contributions totaled more than \$8.2 million over this period, with annual amounts ranging from \$1,250,000 to \$2 million (Regional. "Press"). Over the entire FY 2002 to FY 2011 period, funding by state and local governments for incentives was more than \$42 million.

Almost all the incentive money has gone to AirTran Airways. For FY 2010, the contract between Sedgwick County and AirTran was for the airline to provide three daily round-trip flights—except for two on Saturday—to Atlanta, Georgia. The projected cost to the county for covering AirTran's costs for the year was \$6.5 million. Frontier Airlines began service in October 2007 and has received

¹ Annual funding was \$5 million each year in FY 2007, FY 2008, FY 2009, and FY 2011; and \$4,875,000 in FY 2010.

\$1.5 million in total revenue guarantees through FY 2011 to provide daily round-trip flights to Denver, Colorado (Regional. “Kansas”).

According to a report by Wichita State University, the economic impact for the 2002 to 2007 period of AirTran’s flights was more than \$15 million for Wichita, more than \$7 million for the county, and more than \$107 million for the state. The direct and indirect effects are based on the economic activity generated by AirTran employees, the increase in business at the airport, and savings from decreased ticket prices.

Estimated Economic Impact. The Wichita Airport Authority contracted with Wichita State University’s Center for Economic Development and Business Research to do an economic analysis of the impact of AirTran Airways. The 2008 report is widely cited in discussions about potential incentive programs. According to the report, the impact for the 2002 to 2007 period of the added AirTran service was more than \$15 million for Wichita, more than \$7 million for the county, and more than \$107 million for the state (Harrah 5). The direct and indirect effects are based on the economic activity generated by AirTran employees, the increase in business at the airport, and savings from decreased ticket prices.²

Wyoming

The Wyoming legislature created the Air Service Enhancement Program in 2003. Beginning with FY 2004, the legislature has appropriated \$1.5 million annually. With local matching included, total available funding since FY 2004 is more than \$18 million. Most funding has been used for incentive payments from airports to air carriers, often to provide service during winter months. Funds have also been used for marketing and facilities enhancement. The seven-member Aeronautics Commission, which is part of the Department of Transportation, decides which projects submitted by Wyoming’s airports should be awarded funding and how much local matching funding is required.

Wyoming has a large land area but a population of just less than 545,000. In 2003, finding that a comprehensive system of air travel was needed and that the lack of competition among air carriers resulted in limited, unreliable, and expensive service, the legislature created the Air Service Enhancement Program. Beginning with fiscal year 2004, the legislature has appropriated \$1.5 million annually. Total available funding since FY 2004, including local matching, is more than \$18 million. Most funding has been used for incentive payments from airports to air carriers, often to provide service during winter months. Funds have also been used for marketing and facilities enhancement.

The Aeronautics Commission, which is part of the Department of Transportation, decides which projects submitted by Wyoming’s airports should be awarded Air Service Enhancement funding and how much local matching funding is required. The seven commissioners, who serve 6-year terms, are appointed by the governor with approval by the Senate. The state is divided into five districts, each of which selects a commissioner. Two commissioners are at large (State of Wyoming).

² The estimate of the increased airport activity attributable to AirTran is based on the assumption that the presence of the new airline was responsible for 70 percent of the increased airport activity. The savings in airfares is based on the assumption that Wichita’s fares would have remained 22.75 percent higher than the national average as was the case in the third quarter of 2000 (Harrah 12, 14-15). Savings per ticket based on this assumption has varied by year, ranging from \$94 in 2003 to \$6 in 2006.

For each project selected, there is a maximum funding commitment by the state and the community. According to information provided by the commission, the amounts have ranged from less than \$10,000 for an equipment purchase to \$1.4 million for a revenue guarantee to an airline. Over the period beginning with FY 2004, the Aeronautics Commission has approved maximum funding commitments of \$14.2 million of state funding, matched by community commitments of \$4.7 million. Because much of the funding is in the form of revenue incentives to airlines and not all the incentive money is used, actual state payments have been \$8.5 million over the entire time period. Total community payments were \$2.2 million (Schlabs).

Proposed State Incentive Programs

South Carolina

A bill introduced in 2010 but not enacted by the South Carolina General Assembly would have created the Air Service Incentive and Development Fund to be administered by the Aeronautics Commission. The goals of the program were to provide more flight options, more competition for air travel, and more affordable fares. The bill authorized the Aeronautics Commission to borrow up to \$15 million from the Insurance Reserve Fund for the Air Service fund.

In the 2010 session of the South Carolina General Assembly, H. 4343 passed the House of Representatives but not the Senate. The bill would have created the South Carolina Air Service Incentive and Development Fund to be administered by the Aeronautics Commission. The goals of the program were to provide more flight options, more competition for air travel, and more affordable fares. The fund, which is not to exceed \$15 million, may be funded by annual appropriations from the General Assembly. The bill authorized the Aeronautics Commission to borrow up to \$15 million from the Insurance Reserve Fund for the Air Service fund.³ Money borrowed from the Insurance Fund was to be repaid with interest. For any future fiscal year in which aircraft property tax revenues exceeded \$6 million, the excess would go to the Insurance Fund. Once the loans to the Insurance Fund have been repaid, annual tax revenues from this source that exceeded \$6 million would go to the Air Service fund. The bill does not specify what happens if aircraft property tax revenues are frequently less than \$6 million per year.

Before the fate of the bill was decided, Southwest Airlines announced that it would begin service from two South Carolina airports in 2011 without any proposed state and county subsidies.

According to media reports, the bill was perceived by many as a mechanism to entice Southwest Airlines to begin operating at the Charleston International Airport and the Greenville-Spartanburg International Airport. Opposition by senators from the Midlands area of the state, in which Columbia Metropolitan Airport is located, was reportedly key to the bill not being voted on by the full Senate before the session adjourned (Fitts).

³ The Insurance Reserve Fund is for property and liability insurance for state and local agencies.

Before the fate of the bill was decided, Southwest announced that it would begin service from Charleston and Greenville-Spartanburg in 2011 without any proposed state and county subsidies. It is still possible, however, that incentives from either or both of the two airports will be used by the airline (Frampton).

Louisiana

A bill introduced in but not enacted by the 2010 Louisiana legislature would have created an Air Service Fund that would receive \$9 million each year from existing state aviation fuel tax revenue.

Louisiana House Bill 1413 from the 2010 Regular Session would have created an Air Service Fund. The bill was assigned to a House committee, but there was no further action. The fund would receive \$9 million each year from existing state aviation fuel tax revenues. Unspent funds carry over from year to year, but the total unencumbered balance cannot exceed \$30 million. The money in the fund may be spent only to enhance or increase air service at commercial airports through awards made by the Department of Transportation and Development to specific projects. No project may cost more than \$3 million per fiscal year. The bill would also have created an airport “Construction Acceleration Fund” to be funded with \$3.2 million per year from the existing state aviation fuel tax.

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Appendix A

Letter From Officials of the Kenton County Airport Board, Louisville Regional Airport Authority, and Blue Grass Airport

September 24, 2010

Senator John Schickel, Co-chair
Representative Kelly Flood, Co-chair
Program Review and Investigations Committee

Dear Senator Schickel and Representative Flood:

We appreciate the opportunity to jointly submit comments to the Program Review Committee staff for their use and inclusion into the report they are preparing to present to the Committee, which will evaluate issues and challenges facing the airport industry and to research possible air service enhancement programs.

Our coalition testified before the Interim Joint Economic Development Committee and Program Review Committee last month to present our thoughts and ideas on the challenges to maintaining top quality air service at the state's three main airports. At that committee meeting, Members asked that we collaborate and recommend an approach the legislature might consider to help airports enhance and retain air service.

We have developed three specific suggestions we believe will be beneficial to all commercial airports in the state. Those three items are (1) the use of a TIF program for air service development, (2) the establishment of a revolving loan fund, and (3) allowing airport boards to establish separate commercial operating units for the purpose of providing services to airlines at a lower cost. Each of these items is discussed individually below.

TIF Program

Kentucky's TIF statutes do provide a mechanism to access state revenues to support projects in local TIF districts. However, none of the three state programs that exist under current law provide the type of incentives needed to promote new airline service. We suggest consideration of expanding current TIF statutes to provide eligibility for new service. The following could be considered:

1. The eligibility of state participation in local TIF projects is based on a project with minimum capital investment starting at least \$10 million, with the major State revenues of sales and income taxes available only for projects with a minimum capital investment of \$20 million. The large capital investment requirement does not provide assistance for the attraction of new airline service.

2. Under current law, state TIF revenues may only be used to fund capital costs defined as approved public infrastructure costs. There is no provision for state TIF revenues to be used to fund a program or service to assist airlines in defraying costs to enter a new market.

3. Local and state revenues that are available to be pledged to support a TIF district are based on an incremental increase in taxes from new development within the TIF district. The taxes currently available to support a TIF district may need to be expanded to include fuel taxes and other taxes that are generated by the airline industry.

Revolving Loan Fund

The State could establish a revolving loan fund through the issuance of bonds. These funds would be held in an account for air service development and enhancement purposes only. An initial amount as low as \$5 million could have positive benefits. A maximum amount each airport could access would need to be established. The loan made would carry zero interest and would require a repayment over a relatively short term like 5 years.

Eligible expenses could be for the purchase of ground support equipment, installation of computer cables and other terminal related up-fit costs, the purchase of marketing items such as newspaper, T.V. and radio advertising and for providing capital to an airport operator to fund landing fee abatement and terminal lease abatement for a period of time. This time period could mirror the FAA's abatement period which currently stands at two years.

Other uses for loan proceeds could also be considered, such as a back stop to a revenue guarantee for an airline starting up new qualifying service. A similar strategy is used in Kansas and South Carolina.

Establishment of Separate Commercial Operating Units

Some airport boards are exploring the use of a separate or special commercial operating unit to perform aeronautical services and provide equipment and space for airlines as a means to attract routes to the area. The services provided by the special commercial operating companies are baggage and cargo handling, custodial and parking. The airport can provide the services at a lower cost through a private company, rather than with governmental employees subject to Kentucky Retirement System statutes. Airlines are able to establish routes with very little investment utilizing the space and services provided by the airport.

This is an innovative, outside-the-box suggestion that has brought success in other states such as Missouri, Illinois and Texas.

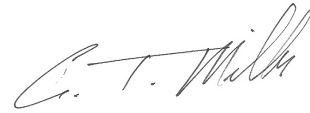
In addition to the above three items, we request the committee include in their assessment of any air service development program the economic value of international air service to the Commonwealth and include the special needs of supporting international air service as a component of the overall program.

Thank you for considering these issues, which we believe will increase Kentucky's competitiveness and grow the economy. We appreciate the opportunity to offer input and appreciate your work on behalf of the Commonwealth.

Sincerely,



John Mok, CEO, Kenton County Airport Board



Skip Miller, Executive Director, LRAA



Eric Frankl, Executive Director, Blue Grass Airport

Appendix B

Example of an Incentive Program Offered by an Airport

Mineta San José International Airport

Airline Air Service Incentive Program

Mineta San José International Airport is committed to successful partnerships with its airlines that benefit Silicon Valley residents and businesses and that increase the availability of flights at SJC. We have two different air service incentive programs to encourage airline partners to provide flights to unserved and underserved destinations.

Focus City Incentive Program

SJC offers a two-year waiver of fees on all flights to new cities as well as added flights to underserved cities to any airline that chooses to designate San José as a “focus city.”

Under a Focus City agreement with the Airport, an airline would commit to adding at least four new flights each year for two consecutive years. The Airport in turn would waive fees and provide additional support for the new flights during this period.

New unserved markets and underserved markets qualify for fee waivers, but added flights to well-served cities will not receive any incentive waiver. New flights to well-served cities will count toward the number of new flights added each year under the Focus City program.

For example, a focus city airline could add flights to two unserved cities, one to an underserved city, and one to a well-served city to satisfy the requirement for four new flights per year under the incentive agreement between the airline and the Airport.

Underserved cities: Austin, Atlanta, New York-JFK, Minneapolis, Chicago-ORD, Sacramento

Well-served cities: Burbank, Dallas-DFW, Denver, Houston-IAH, Las Vegas, Los Angeles, Ontario, Orange County, Phoenix, Portland, Reno, Salt Lake City, San Diego, Seattle

Flexible Route Incentive Program

This program is designed for flexibility to encourage incremental airline route decisions, and it provides benefits for carriers that add short-haul, medium-haul, or long-haul routes, both to unserved and underserved domestic and international destinations.

1. New short-haul domestic routes/flights: 12 month 100% waiver of fees

Unserved cities: Albuquerque, Eugene, Omaha, Palm Springs, San Antonio, Spokane, Tucson

Underserved cities: Austin, Sacramento

2. New medium-haul domestic routes/flights: 24-month waiver of fees; 100% in first year, 50% in second year

Unserved cities: Baltimore, Boston, Charlotte, Cincinnati, Detroit, Fort Lauderdale, Indianapolis, Kansas City, Memphis, Miami, Milwaukee, Nashville, Newark, New Orleans, Orlando, Philadelphia, Pittsburgh, Raleigh/Durham, St. Louis, Tampa, Washington-DCA, Washington-IAD

Canada: Calgary, Montreal, Toronto, Vancouver

Unserved cities in Mexico, Central America, and Hawaii

Underserved cities: Atlanta, Chicago-MDW, Chicago-ORD, Minneapolis, New York-JFK

3. New short-haul international routes/flights: 24-month fee waiver; 100% in first year, 50% in the second year.

4. New long-haul international routes/flights: 36-month waiver of fees, 100% waiver of fees in first year, 66% in second year, 33% in third year

Unserved cities: Tokyo, Osaka, Seoul, Taipei, Beijing, Shanghai, Hong Kong, Guangzhou, Manila, Ho Chi Minh City, Singapore, Auckland, Sydney, London, Dublin, Paris, Amsterdam, Frankfurt, Munich, Zurich, Rome, Milan, Athens

This list may be modified at any time by the SJC Aviation Director

Source: Mineta San José International Airport. <<http://www.sjc.org/business.php?page=outreach/incentive&subtitle=Business+Outreach+%7C+Air+Service+Incentive>>.

Appendix C

Enacted State Incentive Programs: Kansas and Wyoming

Kansas

The Kansas Affordable Airfare Fund was created by Senate Bill 475 in 2006.

AN ACT concerning economic development; creating the state affordable airfare fund to support certain programs; providing for certain studies and reports.

Section 1. (a) There is hereby established in the state treasury the \$5,000,000 state affordable airfare fund, which shall be known and referred to as the state affordable airfare fund and which shall be administered by the secretary of commerce. In accordance with the provisions of appropriation acts, moneys shall be transferred to the state affordable airfare fund from the state general fund or one or more special revenue funds in the state treasury as specified by appropriation acts. All expenditures from the state affordable airfare fund shall be for the program to provide more air flight options, more competition for air travel and affordable air fares for Kansas, including a regional airport in western Kansas. All expenditures from the state affordable airfare fund shall be made in accordance with appropriation acts upon warrants of the director of accounts and reports issued pursuant to vouchers approved by the secretary of commerce or the designee of the secretary.

(b) The moneys credited to the state affordable airfare fund shall be disbursed as an annual grant by the secretary of commerce to the regional economic area partnership (REAP) and shall be used for the development and implementation of a program to provide more air flight options, more competition for air travel and affordable air fares for Kansas, including a regional airport in western Kansas. Each annual grant shall be matched by moneys received by the regional economic area partnership (REAP) from local units of government or private entities on the basis of 75% from the state affordable airfare fund to 25% from local units of government or private entities.

(c) Annually, beginning by January 15, 2008, at the beginning of each regular session of the legislature thereafter, the regional economic area partnership (REAP) shall evaluate and present a report on the effectiveness of this program to the house of representatives committee on appropriations and the senate committee on ways and means. Commencing with the regular session in 2008, the regional economic area partnership (REAP) shall prepare and submit a report on the expenditures of the state annual grant and local matching moneys under the program and the results obtained for such expenditures to the legislature at the beginning of each regular session.

(d) During the interim between regular sessions of the legislature, commencing with the 2006 legislative interim period, the legislative budget committee shall study and review the activities of the regional economic area partnership (REAP) under the program to provide more air flight

options, more competition for air travel and affordable air fares for Kansas, including a regional airport in western Kansas.

Wyoming

The Air Service Enhancement Program was created by the legislature in 2003.

W.S. 10-3-601. Wyoming air services enhancement; legislative findings; Wyoming aeronautics commission authority to contract for services; requirements.

(a) The legislature finds that an adequate and comprehensive system of air service in Wyoming is vital for economic development within Wyoming. Competition among air service providers within the state is virtually nonexistent and, without competition, services will remain limited and unreliable and high air fares will remain a major impediment to use of air services by Wyoming residents and businesses.

(b) The Wyoming aeronautics commission may enter into agreements to provide financial assistance to persons doing business or who will do business in the state, to economic development organizations within the state, to joint powers boards or to other entities formed to provide for enhanced air service to communities in Wyoming that have or are seeking commercial air service, for the enhancement of air services in the state conditioned upon contractual assurances that specified benefits will accrue to the state through increased air traffic and enplanements. For purposes of this article, "enhanced air service" shall include, but not be limited to, assisting airports in the state with commercial air service to have the appropriate level of state or federal security configuration to accommodate proposed air service and aircraft capacity. Benefits accruing to the state shall include, but not be limited to, increasing the minimum number of enplanements at airports facing a possible loss of federal airport improvement program funding, increasing passenger enplanements at commercial airports in Wyoming, increasing frequency or sustaining flight operations from commercial airports in Wyoming to regional airport hubs, lowering airfares for air passengers and increasing the number of routes flown within the state. The commission shall consult with counties, cities, towns, joint powers boards, airport boards or other entities pursuing air service enhancement before entering into agreements to provide air service enhancement and shall require local funds for the provision of air service enhancement grants. The amount of local funds required for the provision of enhancing air services shall be determined by the commission, taking into account the types of service for which grants are approved, the diverse characteristics of the communities to which air service is contracted for and other considerations examined by the commission.

(c) The commission has primary responsibility and may consult with or delegate to the aeronautics division of the Wyoming department of transportation, Wyoming business council or other entities as necessary, to develop criteria and contracts for financial aid under this section.

(d) All applications for financial aid under this section shall be submitted to the aeronautics commission. The aeronautics commission shall approve or deny the application. The applicant

shall be promptly notified of the decision. In making the decision to approve or deny the application, the commission shall give priority to an applicant whereby:

- (i) The applicant can provide assurances that the enhancement has a reasonable chance of success and will achieve benchmarks specified by the applicant;
 - (ii) Participation by the commission is necessary to the success of the enhancement because funding from other sources for the enhancement is unavailable;
 - (iii) The applicant will use the proceeds of the financial assistance provided under this section only to secure or enhance air services within the state or to market or promote the service for which the financial assistance is granted;
 - (iv) The financial assistance has the reasonable potential in the opinion of the aeronautics commission to create a substantial amount of air travel originating within the state;
 - (v) The applicant has already made or is contractually committed to make a substantial financial and time commitment to the enhancement and local funds are provided to secure a financial grant under this section, in an amount determined by the commission;
 - (vi) The applicant will not pledge financial aid granted pursuant to this section as collateral for any other purpose than is specified in the contract between the applicant and the commission;
 - (vii) The applicant will provide reasonable assurances that within a time specified by the commission, the state shall benefit from its investment by means of commercial airports having sufficient enplanements to retain or reestablish eligibility for federal airport improvement program funding and that commercial airports in the state will receive increased revenues from established passenger facility charges as a result of increased enplanements or from other benefits.
- (e) Before granting any financial aid under this section, the commission shall enter into an agreement with the applicant providing for a benefit to the state which is commensurate with the level of risk and amount of the financial aid, using the criteria specified in paragraph (d)(vii) of this section. The attorney general shall review and approve the contract before the commission enters into any agreement under this section.
- (f) As used in this article, "commission" means the Wyoming aeronautics commission created by W.S. 10-3-101.
- (g) The Wyoming aeronautics commission will establish benchmarks for determining the success of the program.

W.S. 10-3-602. Wyoming air services enhancement account.

(a) The commission shall establish and maintain a Wyoming air services enhancement account under this article to provide the financial aid specified in W.S. 10-3-601 to enhance air services within the state. Any funds deposited in the account shall only be expended by the commission as provided in W.S. 10-3-601 and to administer this article.

(b) Any funds appropriated by the legislature to the account established under subsection (a) of this section shall not lapse as provided by W.S. 9-4-207(a), but shall revert to the air services enhancement account within the highway fund on September 30, 2007.

(c) The commission shall report to the joint minerals, business and economic development interim committee, the joint appropriations interim committee and the air transportation liaison committee no later than September 30, 2005, with respect to the status of the program under W.S. 10-3-601, including any actions taken and funds expended in consideration of, and pursuant to, any contract entered into under W.S. 10-3-601. If any funds are expended under a contract prior to June 30, 2006, the commission shall also report no later than that date and annually thereafter with respect to the performance of any recipient of funds under the contract.

Source: <<http://legisweb.state.wy.us/statutes/statutes.aspx?file=titles/Title10/T10CH3AR6.htm>>.

Appendix D

Proposed State Programs: South Carolina and Louisiana

South Carolina

H. 4343, Regular Session, 2010

Status: Not enacted (introduced January 14; passed House; did not pass Senate)

SECTION 1. Title 55 of the 1976 Code is amended by adding:

CHAPTER 19

Air Service Incentive and Development Fund

Section 55-19-10.(A) There is established within the South Carolina Aeronautics Commission a fund which shall be known and referred to as the South Carolina Air Service Incentive and Development Fund and which shall be administered by the commission. The General Assembly in the annual general appropriations act or in other acts shall provide or appropriate monies for the South Carolina Air Service Incentive and Development Fund which in the aggregate shall not exceed the sum of fifteen million dollars. All expenditures from the fund shall be for a program to provide more air flight options, more competition for air travel and more affordable air fares for this State, including regional airports.

(B) The monies credited to the South Carolina Air Service Incentive and Development Fund shall be disbursed as a grant by the commission to regional economic development entities or air service development task forces as established by law and shall be used for the development and implementation of a program to provide more air flight options, more competition for air travel and more affordable air fares for this State. Each grant shall be matched by monies from the grantee or the local jurisdiction in which it is located, on the basis of seventy-five percent from the South Carolina Air Service Incentive and Development Fund to twenty-five percent from the grantee or the local jurisdiction in which it is located.

(C) Annually at the beginning of each regular session of the General Assembly commencing one year after the effective date of this chapter, the commission shall evaluate and present a report on the effectiveness of this program to the House Ways and Means Committee and the Senate Finance Committee which shall include a summary of the expenditures from the fund and local matching monies received under the program and the results obtained for such expenditures.

(D) Monies in the Air Service Incentive and Development Fund may be carried forward from fiscal year to fiscal year and earnings of the fund shall remain part of the fund.

Section 55-19-20. The Aeronautics Commission shall accept grant proposals on a fiscal year basis within available funds from the governing bodies of regional economic development

entities or air service development task forces to accomplish the purposes of the program in accordance with the following guidelines:

- (1) proposals shall specify how the program will provide more flight options, more competition for air travel, and more affordable air fares for the State of South Carolina. In this regard, an applicant shall demonstrate that due diligence has been conducted with respect to a proposal for funding. Due diligence must be documented with an analysis of feasibility from a professional air service consultant or a letter of intent from a commercial scheduled air carrier;
- (2) proposals shall specify the amount of funding requested through the South Carolina Air Service Incentive and Development Fund and indicate the source of the required local match of twenty-five percent;
- (3) proposals shall specify how the program applicant will document the effectiveness of funding received under this program; and
- (4) proposals also shall specify how expenditures and results from this program and local matching monies will be reported.

Section 55-10-30. (A) Grants from the South Carolina Air Service Incentive and Development Fund must be considered and may be awarded in accordance with the purposes of the program, which are more flight options, more competition for air travel, and more affordable air fares for this State. Selection criteria include the following:

- (1) More air flight options including:
 - (a) number of scheduled, daily nonstop flights by commercial scheduled passenger air carriers to United States destinations;
 - (b) number of scheduled, daily one-stop flights by commercial scheduled passenger air carriers to United States destinations;
 - (c) number of scheduled, daily one-stop flights by commercial scheduled passenger air carriers to international destinations;
 - (d) number of connecting cities by a scheduled commercial passenger air carrier to United States destinations that are ranked in the region's top twenty-five markets in terms of origin and destination passengers;
- (2) More competition for air travel including:
 - (a) number of scheduled, daily nonstop flights by commercial scheduled passenger air carriers to United States destinations served by two or more airlines;
 - (b) number of scheduled, daily one-stop flights by commercial scheduled passenger air carriers to United States destinations served by two or more airlines;

(c) number of scheduled, daily one-stop flights by commercial scheduled passenger air carriers to international destinations served by two or more airlines;

(d) average airfare for scheduled, connecting flights for the region's top twenty-five markets in terms of origin and destination passengers;

(3) More affordable air fares for South Carolina including:

(a) average airfare for scheduled, round-trip, nonstop flights by commercial scheduled passenger air carriers to United States destinations;

(b) average airfare for scheduled, round-trip, one-stop flights by commercial scheduled passenger air carriers to United States destinations;

(c) average airfare for scheduled, round-trip, one-stop flights by commercial scheduled passenger air carriers to international destinations.

(B) In making awards, the Executive Director of the South Carolina Aeronautics Commission must give highest priority to maintaining affordable airfares to eastern and western United States destinations. High priority must be given to United States owned, publicly traded network carriers. Priority also must be given to proposals that impact a majority of South Carolinians.

Section 55-19-40. (A) The South Carolina Aeronautics Commission may borrow up to fifteen million dollars from the Insurance Reserve Fund to fund the South Carolina Air Services Incentive and Development Fund. Any money borrowed from the Insurance Reserve Fund must be repaid as prescribed herein. In any fiscal year following Fiscal Year 2010-2011 in which the annual aircraft property tax revenues collected pursuant to Title 12, Chapter 33, Article 19 exceed six million dollars, the revenues in excess of six million dollars shall be used to repay the Insurance Reserve Fund instead of being paid into the State General Fund. The money borrowed from the Insurance Reserve Fund must be repaid together with interest calculated by the State Treasurer's Office in an amount determined to approximate the lost investment earnings on the monies.

(B) If there are no outstanding loans pursuant to this section or any and all loans entered pursuant to this section have been fully repaid, in any fiscal year in which annual aircraft property tax revenues collected pursuant to Title 12, Chapter 33, Article 19 exceed six million dollars, the revenues in excess of six million dollars shall be paid into the South Carolina Air Services Incentive and Development Fund instead of being paid into the State General Fund.

Louisiana

House Bill 1413, Regular Session, 2010

Status: Not enacted (introduced April 20; assigned to House Committee on Transportation, Highways, and Public Works; no further action)

Abstract: 1413 adds to the definition of “development project.” Provides for an exception for information submitted in the Airport Construction and Development Priority Program process for the Air Service Fund. Creates the Air Service Fund and the Construction Acceleration Fund within the Transportation Trust Fund.

AN ACT

To amend and reenact R.S. 2:801(3) and 802(A)(1)(introductory paragraph) and to enact R.S. 2:802.1 and 802.2, relative to the Airport Construction and Development Priority Program; to provide for definitions; to provide for an exception for information submitted in the application process for the Air Service Fund; to create the Air Service Fund and the Construction Acceleration Fund within the Transportation Trust Fund; and to provide for related matters.

Be it enacted by the Legislature of Louisiana:

Section 1. R.S. 2:801(3) and 802(A)(1)(introductory paragraph) are hereby amended and reenacted and R.S. 2:802.1 and 802.2 are hereby enacted to read as follows:

§801. Definitions

As used in this Chapter, unless the context clearly indicates otherwise, the following definitions shall apply:

* * *

(3) “Construction or development project” means a program of construction or development, either new or continuing, that will be planned and implemented with the primary goal of improving aviation activities in the state. “Development project” shall also mean a program of business development, either continuing or new, that will be planned and implemented with the primary goal of improving air service at commercial carrier airports.

§802. Methodology for airport project evaluation

A.(1) Applications for funding of any airport construction or development project may be submitted by any airport authority, except as provided in R.S. 2:806, and equal consideration shall be given to rural aviation and commercial urban aviation. Applications shall be made to the Department of Transportation and Development by November first of each year, beginning in 1989, for consideration of funding in the following fiscal year, except for the projects already on the priority list for 1989-90, which will be funded in the current year. Applications submitted in accordance with the provisions of this Chapter shall not be subject to the provisions of R.S.

39:61 and 62.* Except as provided in R. S. 802.1, information to be provided in the application shall include but not be limited to the following:

* * *

§802.1. Air Service Fund

A. There is hereby created in the state treasury a special fund to be known as the “Air Service Fund”, hereinafter referred to as “the fund”, within the Transportation Trust Fund. Beginning in Fiscal Year 2010-2011 and each year thereafter, the state treasurer shall credit to the fund nine million dollars derived from state taxes collected and received from aviation fuel and deposited in the Transportation Trust Fund. The monies in the fund shall be used solely for the purposes provided in Subsection B of this Section and only in amounts appropriated by the legislature. Unexpended and unencumbered monies in the fund at the end of each fiscal year shall remain in the fund. The unexpended and unencumbered balance in the fund shall not exceed thirty million dollars and the state treasurer shall cease deposits into the fund until such balance is below thirty million dollars.

B. Monies in the funds shall be used and expended solely for a program that enhances or increases air service at commercial carrier airports through the award of monies for specific projects. No project shall exceed three million dollars in any given fiscal year. For projects for Fiscal Year 2010-2011, applications shall be made to the department by November first of each year. The department, in consultation with the Department of Economic Development shall promulgate and adopt rules and regulations for the implementation of the program. Notwithstanding any provision of law to the contrary, the promulgation and adoption of any rules and regulations shall be in accordance with the Administrative Procedures Act for Fiscal Year 2010-2011 are considered to be an emergency rule. The program shall be subject to the provisions of R.S. 2:803 except that projects for Fiscal Year 2010-2011 shall be followed to the extent practicable but shall be subject to oversight and approved by the joint transportation, highways and public works committee.

§802.2. Construction Acceleration Fund

A. There is hereby created in the state treasury a special fund known as the “Construction Acceleration Fund”, hereinafter referred to as “the fund”, within the Transportation Trust Fund. For Fiscal Year 2010-2011 and each fiscal year thereafter, the state treasurer shall credit to the fund three million two hundred thousand dollars derived from state taxes collected and received from aviation fuel and deposited in the Transportation Trust Fund. The monies in the fund shall be used solely as provided in Subsection B of this Section and, except as provided in Subsection C of this Section, only in amounts appropriated by the legislature. Unexpended and unencumbered monies in this fund at the end of each fiscal year shall remain in the fund.

B. Monies in the fund shall be used and expended solely for a program that accelerates construction of projects within the aviation priority program. Notwithstanding any provision of law or rule to the contrary, no project for a commercial service airport shall not exceed six million dollars. A project for a general aviation airport shall not exceed one million dollars in

any given fiscal year and for projects funded in accordance with this Section there shall not be a specific limitation per commercial service or general aviation airports.

C. The State Bond Commission or its successor may issue and sell bonds, notes or other obligations secured by a pledge of the revenues deposited in the Transportation Trust Fund which after the Bond Security and Redemption Fund have been satisfied in the manner provided in Article VII, Section 27(D) of the Constitution of Louisiana, and if so pledged any portion thereof needed to pay principal, interest, or premium, if any, and other obligations incident to the issuance, security, and payment may be expended by the state treasurer. Any bonds issued in accordance with this Subsection shall be sold in two series with one series beginning in Fiscal Year 2010-2011 and another series ending in Fiscal Year 2011-2012. Thereafter, except for refunding bonds at a lower rate, shall not be issued in accordance with this Section. At such time, all bonds, including refunding bonds, issued in accordance with this Section are paid in full with both principal and interest, the fund shall be abolished and the authority contained herein shall become null, void, and have no effect.

Appendix E

How This Study Was Conducted

At its June 2010 meeting, the Program Review and Investigations Committee voted to initiate a study of economic incentives to airlines and airports. Reductions in commercial air service, particularly at the Cincinnati/Northern Kentucky Airport, raised concerns about local job losses and future economic development within the region and state.

To complete this study, Program Review staff reviewed federal and state statutes and regulations, compiled and analyzed aviation statistics, reviewed the relevant literature, and examined economic incentives provided to airlines and airports in other states. Program Review staff also conducted interviews with officials and staff from the Cincinnati/Northern Kentucky, Louisville, Lexington, Paducah, and Owensboro commercial airports; Northern Kentucky Chamber of Commerce; Wyoming Department of Transportation; Mobile Airport Authority; and the US Federal Aviation Administration.

