

SHORTCHANGED

How Airlines Can Repay Taxpayers for Billions in Subsidies by Improving Jobs, Security and Services



Carolina Briones
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Los Angeles Alliance for a New Economy
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EXECUTIVE SUMMARY

Developed and nurtured with taxpayer dollars, the airline industry holds a special status in the United States. From the early days of flight up through the early 1970s, the U.S. government provided more than \$155 billion in direct support for the aviation industry. Even after the industry was deregulated in the 1970s, federal and local governments have continued to play a crucial role in supporting the industry by providing infrastructure support, tax exemptions, and low-cost financing. The justification given for the government's investment in the industry has been the crucial role the airlines play in facilitating commerce, providing jobs, and bringing the inhabitants of a vast continent closer together.

More recently, the terrorist attacks of 9/11 brought financial devastation to the industry and provided a compelling rationale for increased government subsidies. After 9/11, the federal government not only provided the airlines with billions in cash grants, but also increasingly took on some of the economic risks associated with the industry's operations, by acting as the airlines' insurer, providing loan guarantees, and taking responsibility for airline employee pensions. Even after the industry returned to profitability in 2006 and 2007, it continued to benefit from some of these federal subsidies.

Table E-1: Public Subsidies Provided to the Airline Industry

Assistance Program	Description of Subsidy	Estimated Value of Subsidy Received
Post 9/11 Federal Subsidies		
Cash Grants	\$4.64 billion in taxpayer funds	\$4.64 billion
Loan Guarantees	\$1.65 billion in guarantees in case of airline loan defaults	Not available
War Risk Insurance	FAA took over from the private sector the role of providing war risk insurance to the airlines after 9/11	\$340 million per year in industry cost savings
Pension Bailouts	Pensions for nearly 240,000 airline employees assumed by federal corporation	Not available
Pension Reform Legislation	Federal legislation that eased pension requirements for airlines, but did not involve a government expenditure	\$3 billion in industry cost savings
Total Federal		\$7.98 billion
State and Local Subsidies in California		
State and local sales tax exemption on jet fuel	An estimated \$800 million over the five-year period from fiscal year 2005 to 2009	\$473 million through current fiscal year
United Airlines local sales tax reduction agreement with City of Oakland	\$13.7 million in business incentive payments from 2004 to 2007	\$13.7 million
Bond financing at LAX and SFO	\$1.7 billion in low-interest financing since 1970	Not available
Total in California		\$486.7 million
TOTAL		\$8.47 billion

The airline industry now faces another financial crisis brought on by skyrocketing oil prices, which may lead to fundamental industry restructuring and renewed calls for aid. Now more than ever, it is important to ensure that subsidies to the industry result in significant benefit to the public, in the form of good jobs, passenger safety, and quality service.

This report will show that the airline industry is currently failing to provide an adequate return on the public's investment, due to substantial declines in job quality and service quality in recent years. Wages and benefits in the industry have been severely eroded by airline outsourcing and by cuts in compensation for in-house employees since 9/11. Taxpayers foot the bill twice when low-wage uninsured workers are forced to rely on government assistance programs. Moreover, airline cost-cutting and contracting out of critical duties without adequate standards have jeopardized security and passenger safety, while airline service quality ratings have fallen to their lowest level in history.

The airline industry has received an estimated \$8 billion in federal assistance since the 9/11 attacks, with few strings attached. Even after the industry returned to profitability in 2006 and 2007, airlines continued to benefit from several of these subsidies.

- ▶ In the immediate aftermath of the attack, the federal government provided the airlines with \$4.6 billion in cash grants, with virtually no strings attached.

- ▶ The airlines also took advantage of \$1.65 billion in loan guarantees from the federal government, enabling them to obtain commercial financing they could not have otherwise.
- ▶ In addition, the federal government took over from the private sector the role of providing war risk insurance to more than 70 airlines, resulting in an estimated annual savings to the industry of \$340 million. Although this arrangement was intended as a temporary measure, the program has been extended every year since it began.
- ▶ Since 9/11, a federal corporation has assumed responsibility for 16 underfunded airline employee pension plans covering nearly 240,000 employees. This was a major cause of the agency's spiraling deficit in 2004 and 2005, raising concerns about a taxpayer bailout of the agency. The deficit also resulted in premium increases for the agency's users, forcing other companies to subsidize airlines and other companies that had underfunded their pensions.
- ▶ Federal pension reform legislation passed in 2004 and 2006 intended to tighten loopholes also provided relief to the airlines valued at more than \$3 billion. This relief did not involve a government expenditure of funds.

Since 2002, the airlines have received an estimated \$487 million in state and local subsidies in California, including tax exemptions and low-interest bond financing.

- ▶ Unlike motorists and other fuel users in California, airlines are exempt from state sales taxes on their purchases of jet fuel for some flights. The state Board of Equalization estimates that the airlines' tax exemption for international flights will cost the state and local governments more than \$800 million over a five-year period from fiscal year 2005 to 2009.
- ▶ The airline industry has lobbied repeatedly to expand this sales tax exemption to fuel purchases for out-of-state domestic flights, which would cost taxpayers millions more.
- ▶ In 2002, United Airlines entered into an agreement with the City of Oakland that allowed the airline to avoid paying \$13.7 million in local jet fuel sales taxes over a four year period.
- ▶ Since 1970, airlines at LAX have received approximately \$1.3 billion in low-interest bond financing to construct or improve facilities or to purchase equipment. United Airlines has also received additional low-interest bond financing totaling nearly \$413 million for improvements to facilities at LAX and SFO.

Traditionally, the airline industry has provided middle-class jobs that enable workers to provide for their families, receive health care when they need it, and retire in dignity. However, the airlines have severely eroded job quality in the industry through contracting policies that drive down wages and benefits and by economic concessions forced onto airline employees after 9/11.

- ▶ An analysis of wages for 5,000 contracted airline service workers at four major airports in California shows they earn less than they need to be self-sufficient. Health benefits are unavailable or unaffordable for most of these workers. Conditions are likely to be the same for the estimated 18,000 contracted airline service workers at airports throughout California.
- ▶ California taxpayers bear the cost when low-wage uninsured workers rely on government assistance programs and overtaxed public health care facilities and hospital emergency rooms.
- ▶ In Los Angeles, airline service jobs contribute to poverty in many of the communities most affected by pollution and noise impacts from LAX.
- ▶ Airlines have cut wages and benefits for in-house employees so much that, according to the *Wall Street Journal*, "a growing number of airline jobs are more akin to those at a fast-food restaurant." Major airlines have shed more than 170,000 employees in the five-year period after 9/11, which represents a loss of 38 percent.



Airline cost-cutting and contracting out of critical duties without adequate standards have jeopardized security and passenger safety. Meanwhile, airline service quality ratings have fallen to their lowest level in nearly two decades.

- ▶ An April 2007 survey of airline contracted workers at LAX showed that airlines were compromising security by failing to ensure adequate training for workers with security duties. A January 2008 survey of similar workers at San Jose International revealed the same problems.
- ▶ The same LAX survey showed that airlines were not providing adequate services to the elderly and to passengers with disabilities because of equipment problems, lack of

training, and understaffing. In addition, workers reported that public health was threatened by inadequate cleaning of airplane cabins.

- ▶ Earlier this year, the FAA directed airlines to ground hundreds of planes upon discovering gaps in inspection and maintenance.
- ▶ The 2008 Airline Quality Rating report gave the industry its lowest scores since rating began nearly two decades ago. The annual report is released by the Aviation Institute at the University of Nebraska and compiles statistics from the Department of Transportation on denied boardings, on-time flights, mishandled baggage, and customer complaints.

Conclusion and Recommendations

The airline industry has benefited greatly from taxpayer support, and the public has a right to insist on a fair return for its investment. Instead, the industry has eroded job quality for its in-house and contracted employees. When low-wage workers in the industry rely on public assistance programs and public health care facilities, the airlines are doubly subsidized. Declines in job quality affect employee productivity, retention, and morale, leading to further service declines.

While the industry recovered financially from 9/11 in 2006, it now faces another financial crisis. The airlines should not view their current challenges as a justification for further erosion of job quality and service standards. Instead, the industry should

recognize that investing in its workforce and improving service quality are essential steps towards long-term industry success and profitability. In order to improve conditions in this industry, both the airlines and the public sector must take action.

1. **The airline industry should provide a fair return on the public's investment by providing middle-class jobs and ensuring quality service and passenger safety.** The airline industry should provide jobs with adequate wages, benefits and training to both its contracted and in-house employees. Studies have shown that improving compensation for low-wage workers improves their productivity. According to MIT Professor Tom Kochan's research on the airline industry, improving employee compensation and labor relations will ultimately lead to higher airline productivity and profitability.¹



Improvements in training and retention will also lead to better service quality and security for passengers. A recent J.D. Powers report on the industry found that, “In this unstable industry environment, it is critical that airlines invest in their employees as a means to enhance the customer experience, as there is a strong connection between employee satisfaction and customer satisfaction.”²

2. **Federal, state, and local officials should take action to raise standards for job quality, security and service quality in this industry.** LAX has recently approved a policy to raise standards for airline contracted workers, and San Jose airport is considering extending its living wage policy to cover the same workforce. SFO has various policies that set standards for employee minimum compensation and health care coverage, but most airline contractors are not consistently covered by all policies. SFO is currently reviewing

these policies with a goal of developing a consistent standard that improves conditions for airline contracted workers. The California legislature is considering two bills to expand passengers’ rights, AB 1407 and AB 1943, which would improve protections for passengers on delayed flights. Congress should move forward on a federal passenger bill of rights, which would provide uniform protections across the nation.

3. **Government programs that provide subsidies to business should contain public benefit requirements.** Job and service quality standards should be attached to subsidies at the federal, state and local levels. Even further, the federal government should view decisions that provide economic benefit to the airlines—such as airline merger approvals and changes to industry fees that fund FAA operations—as opportunities to demand improvements from the industry.



CHAPTER 1: INTRODUCTION

Developed and nurtured with taxpayer dollars, the airline industry holds a special status in the United States. From the early days of flight up through the early 1970s, the U.S. government provided more than \$155 billion in direct support for the aviation industry, according to the Congressional Research Service.³ Even after the 1970s—when the industry was deregulated—federal and local governments continued to play a crucial role in supporting the industry by providing infrastructure support, tax breaks, and low-cost financing. The government’s investment in commercial aviation has been justified by the crucial role the airlines play in facilitating commerce, providing jobs, and bringing the inhabitants of a vast continent closer together.

While airport security has always been a prime concern, it became a front burner issue in the aftermath of 9/11, when four commercial airliners were used in deadly terrorist attacks. The federal government responded with great speed to requests by the industry to provide billions of dollars of assistance to address the economic fallout of 9/11. Even after the airlines returned to profitability in 2006 and 2007, they continued to benefit from several key post-9/11 subsidies.⁴ In the past several decades, California state and local agencies have also been forthcoming with hundreds of millions of dollars in tax breaks and low-cost financing.

The airline industry now faces another financial crisis brought on by skyrocketing oil prices, which may lead to fundamental industry restructuring

and renewed calls for aid. In 2008, several airlines have filed for bankruptcy and industry merger talks have begun. Now more than ever, it is important to ensure that subsidies to the industry result in significant benefit to the public, in the form of good jobs, passenger safety, and quality service. Though the financial challenges currently faced by the industry are serious, they should not be a justification for low-wage jobs without health benefits and declines in safety and service quality. Instead, the industry should recognize that investing in its workforce and improving service quality are essential steps towards its long-term success and profitability.

Unfortunately, the airlines have taken the opposite approach. This report will show that the airlines have failed to live up to their responsibility to provide adequate training and quality jobs to workers. This failure has impacted passenger safety, service quality and public health. Airline employees—flight attendants, mechanics, ramp workers, and pilots—have seen their wages cut and their pension plans eviscerated. At California’s airports—and at airports across the country—airlines contract out critical services to companies that provide the lowest bid. Without proper standards in place, this approach erodes job quality and can put the public in jeopardy.

The need for safety and quality service at our nation’s airports may be reason enough for policymakers to address the issue of the lack of adequate contracting standards and eroding job quality for in-house employees. The crisis of

low-wage poverty in California should also be a compelling motive for local officials to address the negative consequences of the airlines' cost-cutting strategy. One in five of California's 9.3 million working families had incomes below 200 percent of the federal poverty line in 2005 and lacks the income to pay for basic necessities.⁵ This report argues that the extent of taxpayer support for the airlines constitutes a powerful rationale for demanding safety and accountability from the air carriers.

The point of this analysis is not to condemn taxpayer involvement in supporting the airlines, but rather to make clear the extent to which the airlines depend on the public sector and the public's right to demand accountability in return.

Based on a review of government documents and press reports, as well as interviews with workers, this report provides a detailed examination of post-9/11 federal assistance and an accounting of ongoing subsidies from California's state and local government agencies. In all, the airlines have received billions of dollars in taxpayer support through direct grants, pension bailouts, subsidized insurance, and tax breaks. While much of the assistance was a response to the severe financial impacts of 9/11, it appears that the crisis provided an opportunity for the airlines to seek aid for pre-existing financial problems. Furthermore, some of that assistance continued even after passenger traffic rebounded and surpassed pre-9/11 levels

in 2005, and after the industry returned to profitability in 2006 and 2007.⁶ The point of this analysis is not to condemn taxpayer involvement in supporting the airlines, but rather to make clear the extent to which the airlines depend on the public sector and the public's right to demand accountability in return.

The Impacts of Airline Deregulation on Service Quality and Passenger Safety

Of course, airline operations in California—and across the country—have been affected by industry restructuring. In 1978, the airline industry was deregulated through federal legislation. Deregulation offered some benefits to consumers. Ticket prices dropped significantly and price competition increased.⁷ But deregulation also had some negative consequences for passengers and has led to periods of crisis and instability for the industry. From 1978 through 2005, 162 airlines filed for bankruptcy.⁸

One of the main architects of airline deregulation has conceded that although consumers have benefited from lower ticket prices, "The skies have become more crowded and airlines may, under pressure of competition, have cut corners."⁹ Labor costs have been a major focus for the industry's cost-cutting.¹⁰ According to the *Wall Street Journal*, airlines have cut wages and benefits so much that they are having problems with recruitment and retention of employees. Airlines have cut costs by demanding givebacks from highly skilled direct employees, reducing both pay and

pension benefits of pilots and flight attendants, often with the help of bankruptcy protections. Major network carriers cut more than 170,000 workers, or 38 percent of the total workforce, between August 2001 and October 2006, according to the Air Transport Association.

Since deregulation, many functions that used to be performed by airline employees have been contracted out to companies paying lower wages and benefits. The devastating impact of United Airlines' outsourcing of airplane maintenance jobs on Indianapolis workers and their families was well-documented in *New York Times* reporter Louis Uchitelle's *The Disposable American: Layoffs and their Consequences*.¹¹ Uchitelle describes how, after receiving \$320 million in subsidies from the city and state to pay for the construction of a state-of-the-art maintenance facility, United Airlines closed the plant and replaced their own employees with lower-paid subcontracted workers.

The outsourcing of maintenance work has also created serious concerns about the safety of airlines.¹² At least 64 percent of airline maintenance work is now being performed by outside contractors, many of them not certified by the Federal Aviation Administration (FAA)¹³. The issue of outsourcing and cost-cutting surfaced earlier this year when the FAA directed airlines to ground hundreds of planes upon discovering gaps in inspection and maintenance. Concerned about the quality of work being done, the Department of Transportation's Inspector General has recommended that the FAA strengthen its

oversight of the airlines' use of these contractors.¹⁴

The National Transportation Safety Board found that two devastating airplane crashes resulting in the deaths of hundreds of passengers—the 1996 ValuJet crash and the 2003 US Airways Express crash—were caused by improper maintenance carried out by subcontracted workers.¹⁵ An investigation found that only one-third of the subcontracted workers hired by ValuJet's contractor Sabratech were properly licensed.¹⁶

The Impact of Airlines' Cost Cutting on California

California's airports are major destinations for tourists, business travelers and passengers catching connecting flights to Asia and the Pacific Rim. In 2005, 177.9 million passengers traveled through California's commercial service airports. In all, the California aviation industry accounts for 9 percent of state GDP and generates \$14.5 billion in tourism dollars. The state accounts for 12 percent of the nation's travel market.¹⁷

California's airports are major destinations for tourists, business travelers and passengers catching connecting flights to Asia and the Pacific Rim.

The impact of airline cost cutting has been felt by passengers and in communities throughout the California. LAANE’s 2007 study of Los Angeles International Airport found that the airlines’ contracting policies were jeopardizing public safety, undermining the quality of service to passengers, and providing substandard jobs.¹⁸ Likewise, a 2008 Working Partnerships USA report found that airline service workers charged with critical security and public safety responsibilities at Norman Y. Mineta San Jose International Airport were being paid poverty wages and receiving insufficient training.¹⁹

These two reports are only the most recent to examine the degree to which the lack of adequate standards for airline contracting has harmed the quality of services provided to passengers and jeopardized their safety.²⁰ A 2000 General Accounting Office report found that airport screener performance—which at the time was provided by airline contractors—was impaired by a lack of training and high turnover rates, which pose significant risk to airport security.²¹ After 9/11, airport screeners became employees of the federal Transportation and Safety Administration, but many critical security-related airport functions were left in the hands of private security contractors.

Not surprisingly, as job quality has declined, airline service quality has suffered. The Airline Quality Rating (AQR) report, released by the Aviation Institute at the University of Nebraska, compiles statistics from the Department of Transportation

on denied boardings, on-time flights, mishandled baggage, and customer complaints, including those from passengers requiring wheelchairs. In 2007, the industry as a whole scored the worst Airline Quality Rating ever recorded since the annual report began nearly two decades ago.²²

Fortunately, efforts are underway in four California cities to improve the training and compensation of these crucial workers. In Los Angeles, San Francisco, Oakland, and San Jose, contracted airline service workers are joining with community groups, disability advocates, clergy, and elected officials to raise job quality, training and service standards. These four airports account for 67 percent of commercial airport traffic in California and are the focus of active efforts to improve training and raise standards for private service contractors.²³ In all, they employ an estimated 12,200 airline contracted service workers. Table 1-1 shows the number of workers at the four airports.²⁴

Table 1-1: Contracted Airline Service Workers at Four Major California Airports

Airport	Estimated Number of Airline Contracted Service Workers
LAX	6,500
SFO	3,000
OAK	1,500
SJC	1,200
Total	12,200

Source: Los Angeles World Airports, Service Employees International Union

Outline of the Report and Methodology

Based on a review of government documents, journal articles and press reports, Chapter 2 details the post-9/11 federal support to the commercial carriers, including subsidized insurance, low-cost financing, grants and pension bailouts. Chapter 3 details financial subsidies from California state and local agencies, including local tax breaks and below market rate bond financing at California's two largest airports, LAX and SFO.

For this report, quantifying the cost or value of subsidies is addressed in several ways. In the case of direct cash payments, the actual cost of the subsidy to taxpayers has been documented by a government agency. In other cases, the cost to taxpayers or the value to the industry has been estimated by sources such as government agencies,

major newspapers, or the industry itself. In some cases, estimating the value of the subsidy is beyond the scope of this report. The dollar amounts of subsidies have not been adjusted for inflation. Since most of the subsidies were given in the past, adjusting for inflation would have increased the estimate of the dollar amount of the subsidy.

Chapter 4 assesses the quality of airline service jobs in the state, based on the previously released surveys of workers at LAX and San Jose International Airport, as well as a review of local wage policies and union contracts. Chapter 5 draws on the LAX and San Jose surveys to explore how poor job quality and lack of training undermine passenger safety and security. Finally, Chapter 6 provides conclusions and recommendations for local policymakers and for the airline industry.



CHAPTER 2: FEDERAL GOVERNMENT SUPPORT OF THE AIRLINES POST-9/11 AND BEYOND

- ▶ The airline industry has received an estimated \$8 billion in federal assistance since the 9/11 attacks, with few strings attached. Even after the industry returned to profitability in 2006 and 2007, the airlines continued to benefit from several of these subsidies.
- ▶ In the immediate aftermath of the attack, the federal government provided the airlines with \$4.6 billion in cash grants, with virtually no strings attached.
- ▶ The airlines also took advantage of \$1.65 billion in loan guarantees from the federal government, enabling them to obtain commercial financing they could not have otherwise.
- ▶ In addition, the federal government took over from the private sector the role of providing war risk insurance to more than 70 airlines, resulting in an estimated annual savings to the industry of \$340 million. Although this arrangement was intended as a temporary measure, the program has been extended every year since it began.
- ▶ Since 9/11, a federal agency has assumed responsibility for 16 underfunded airline employee pension plans, covering nearly 240,000 airline employees. This was a major cause of the agency's spiraling deficit in 2004 and 2005, raising concerns about a taxpayer bailout of the agency. The deficit also resulted in premium increases for the agency's users, forcing other companies to subsidize airlines and other companies that had underfunded their pensions.
- ▶ Federal pension reform legislation passed in 2004 and 2006 intended to tighten loopholes also provided relief to the airlines with a value estimated at more than \$3 billion. This relief did not involve an expenditure of government funds.

The terrorist attacks of September 11, 2001, were a devastating blow to an already ailing industry. The event triggered an immediate outpouring of federal assistance to the airline industry, accompanied by major shifts in aviation policy and law. Nobel laureate Gary S. Becker told *Business Week* in November 2001: "The airlines used the attacks as justification for large federal subsidies,

and Congress responded."²⁵ Today the industry continues to benefit from several key subsidies initiated in response to the 9/11 crisis, including a federal corporation's takeover of airline employee pension funds, legislation granting the airlines pension relief, and the FAA's war risk insurance program. This support has continued despite the industry's return to profitability in 2006 and

2007. Following the attacks, national passenger traffic rebounded and surpassed pre-9/11 levels in 2005, which led to industry-wide profits of \$3 billion in 2006 and \$5 billion in 2007, according to the Air Transport Association (ATA), the airlines' trade group.²⁶

Nobel laureate Gary S. Becker told *Business Week* in November 2001: “The airlines used the attacks as justification for large federal subsidies, and Congress responded.”

It is widely acknowledged that the airline industry was ailing prior to 9/11. The major network carriers, such as United and American, were suffering from increased competition by low-cost carriers, such as JetBlue and Southwest. Other challenges included competitive pricing due to the Internet market, and a sharp drop in business demand

(41 percent in the first six months of 2001²⁷). Industry analysts had projected industry-wide annual losses of \$2 to \$3 billion for 2001 even before the attacks,²⁸ and many carriers were already in the process of negotiating loans to preserve their liquidity through the downturn.²⁹ As Senator Fritz Hollings (D-South Carolina), then chairman of the Senate Commerce Committee, said in late September 2001: “The airlines told us they were going broke long before these attacks occurred, while at the same time giving their executives \$120 million in salaries and bonuses this year.”³⁰

Distinguishing between pre- and post-9/11 losses, therefore, was no easy matter, nor can the actions of the airlines in the wake of the disaster—such as invoking *force majeure* clauses to fire tens of thousands of workers—be seen as purely emergency measures. It is an industry with a long history of reliance on government support, and its fate was already hanging in the balance. Below we provide the detail of federal assistance to the airlines.



CASH GRANTS TO AIRLINES

The most direct subsidy to the airlines after 9/11 came in the form of cash grants totaling \$4.6 billion, issued with virtually no strings attached.³¹ Table 2-1 itemizes the largest grants made to the airlines after 9/11. Federal law stipulated that this relief was intended to compensate carriers for: 1) direct losses incurred due to the federal ground stop order issued in the days following the attacks, and 2) incremental losses accrued through December 31, 2001.

Table 2-1: Largest Cash Grants Made to Airlines After September 11, 2001

Carrier	Total Compensation (in millions)
United Airlines	\$774.2
American Airlines	\$693.9
Delta Airlines	\$635.7
Northwest Airlines	\$428.1
Continental Airlines	\$361.5
US Airways	\$306.9
Southwest Airlines	\$282.8
TWA Airlines	\$144.1
America West Airlines	\$116.7
Federal Express	\$100.7
United Parcel Service	\$81.2
Alaska Airlines	\$71.8
American Trans Air	\$50.1
American Eagle Airlines	\$25.5
Total	\$4,073.2

Source: U.S. Department of Transportation

The 14 major carriers claimed losses of \$5.6 billion and ultimately received \$4.1 billion in relief. Of these 14, eight received the entire amount they requested. All told, the government distributed \$4.6 billion to 427 carriers.³² The largest single grant went to United Airlines (\$774 million). American and Delta were close behind with \$694 million and \$636 million, respectively.³³

LOAN GUARANTEES

In addition to the \$5 billion in grants, federal law provided for \$10 billion in taxpayer-backed loan guarantees (also called federal credit instruments), intended to stave off bankruptcy for shaky carriers and help to stabilize the industry. The guarantees required no immediate expenditure of funds—they were not loans in themselves—but rather provided the security necessary for carriers to obtain commercial loans they could not have obtained otherwise. Should any of these carriers default on their loans, however—as one did—the government was liable for the outstanding amount.

The board overseeing the loan guarantees—the Air Transportation Stabilization Board (ATSB)—received sixteen applications in all. It approved seven and ultimately issued six loan guarantees totaling \$1.56 billion.³⁴ Three of these loans were repaid without incident (by Frontier Airlines, Aloha Airlines, and World Airways). Two were sold to private investors without the guarantee when those borrowers—America West Airlines and US Airways—merged in 2005.

The sixth loan, held by ATA Airlines, went into default when the company filed for bankruptcy in 2004.³⁵ The original guarantee was secured for \$148.5 million in 2002, to back a \$168 million loan. The outstanding balance at the time of the company's bankruptcy was \$123.7 million. The ATSB paid this amount, and because ATA's collateral came up short, the government incurred a loss of around \$20 million. To recover the amount, the ATSB then reconfigured the guarantee as a direct loan to ATA for \$125 million. It was finally repaid only when ATA emerged from bankruptcy in 2006.

Table 2-2: Loan Guarantees Issued by the Federal Government

Airline	Guarantee Amount (in millions)	Outcome
America West Airlines (merged with US Airways in 2005)	\$379.6	Loan sold, guarantee obligation cancelled
US Airways (merged with AWA in 2005)	\$900.0	Loan sold, guarantee obligation cancelled
ATA	\$148.5	ATSB paid \$123.7 million when ATA defaulted on loan, ATA later repaid ATSB
World Airways	\$27.0	Loan Repaid
Frontier Airlines	\$63.0	Loan Repaid
Aloha Airlines	\$40.5	Loan Repaid
TOTAL:	\$1,558.6	

Source: Air Transportation Stabilization Board

WAR RISK INSURANCE

The third major branch of federal relief for the airlines came in the form of war risk insurance provided by the federal government, estimated to have saved the industry hundreds of millions of dollars annually.

Prior to 9/11, most air carriers obtained war risk insurance through commercial insurance companies, typically included with a general, all-risk insurance package at little or no extra charge. The insurance covers damage due to any act of war or terrorism, including invasion, insurrection, rebellion and hijacking. It takes three forms: 1) Hull: loss of or damage to the aircraft itself, calculated based on the value of the craft, 2) Passenger liability: death or injury to aircraft passengers, and 3) Third-party liability: losses to anything outside the aircraft.

Commercial Insurance Becomes Unaffordable

Immediately after 9/11, commercial insurers invoked a seven-day cancellation clause to terminate all war risk policies then held. On September 24, 2001, they reinstated those policies at drastically higher rates, with significantly lowered caps for third-party liability. According to Government Accountability Office (GAO) estimates, the total annual cost to the 14 major carriers for this insurance jumped from approximately \$12 million prior to the attacks to \$719 million immediately afterwards.³⁶ Liability caps for third-party coverage, meanwhile, dropped from \$1.5 to \$2 billion per occurrence to \$50 million in aggregate, with up to \$1 billion in excess coverage available for an extra charge of \$1.85 per passenger.³⁷ (Hull and passenger liability caps remained the same.)

Congress Steps In, Increasing Taxpayers Exposure to Risk

Congress addressed the situation through two insurance-related provisions:

1. It provided \$68 million in direct payments to reimburse 183 carriers for the 30 days of increased premiums following the 9/11 attacks.³⁸ (Of this total, \$58 million went to the 14 major carriers.)
2. It expanded the Aviation Insurance Program to provide third-party liability war risk insurance to all domestic carriers whose coverage was canceled. A year later, the Homeland Security Act expanded the program to include hull and passenger liability insurance as well.³⁹

In 2007, the Department of Transportation reported having issued 77 premium war risk policies, with liability for each carrier's claim ranging from \$100 million to \$4 billion per occurrence.⁴⁰ The maximum amount of liability available for both hull loss and liability is \$4 billion, meaning that the government would be liable for up to \$4 billion in damages stemming from any given incident involving a plane that is insured to this degree. The maximum available commercially, by contrast, is around \$1 billion.⁴¹

All claims are to be paid from the Aviation Insurance Revolving Fund, which is financed primarily by premiums collected from carriers and interest on investments in U.S. securities, but has received public funds on at least one occasion.⁴² In October 2001, it received \$50 million of a \$1.7 billion emergency relief package issued by President Bush.⁴³

Given the current liability cap of \$4 billion per occurrence, however, a single disaster could potentially deplete the fund and create political pressure for a taxpayer bailout. As the GAO reported in 2003, the expansion of the FAA's Aviation Insurance Program has increased the government's risk exposure "to as much as \$113 billion for 71 carriers."⁴⁴ The balance in the Revolving Fund at that time, however, was approximately only \$194 million—a difference of \$112.8 billion. Furthermore, according to the most recent GAO report on the matter, the balance in the Aviation Revolving Fund from which claims are paid "may not be sufficient to pay a carrier's claim in a timely manner."⁴⁵

The Aviation Insurance Program's expansion of coverage was intended as a temporary measure to provide reasonably priced insurance for carriers while allowing time for the commercial insurance market to stabilize.⁴⁶ The program has been continuously extended since that time, however, whether by legislative or presidential act. It is currently in place through August 2008, with the possibility of another extension to December 31, 2008.⁴⁷

Hundreds of Millions in Savings to the Airline Industry

As the Secretary of Transportation reported to Congress in 2003: “Presently, there is no economic incentive for U.S. airlines to purchase any commercial war risk liability insurance due to the HSA’s mandatory expansion of the DOT program to include hull loss and passenger liability coverage at rates significantly lower than commercial rates.” (“Report to Congress: Aviation War Risk Insurance,” FAA, March 2003, p.5.)

The airline industry itself acknowledges the substantial value of this subsidy. In June of 2004, Continental Airlines CEO Gordon M. Bethune, speaking to Congress on behalf of the Air Transport Association, said that a conservative estimate of the cost of war risk insurance on the private market was \$600 to \$700 million annually.⁴⁸ In a brief issued in January 2007, the ATA reduced that amount slightly, declaring: “A return to the commercial market to obtain war risk insurance could cost U.S. airlines over \$500 million in premiums annually compared with the

current cost of \$160 million.”⁴⁹ Therefore, the airline industry enjoys an annual savings of at least \$340 million due to this insurance program.

The International Air Transport Association (IATA) has argued that the Aviation Insurance Program puts carriers from nations that don’t have a subsidized program at a competitive disadvantage. According to IATA statistics, U.S. carriers pay less than a quarter of what carriers outside of the U.S. pay for war risk coverage: approximately \$0.70 per passenger, compared with approximately \$3.00 per passenger.⁵⁰

As the GAO reported in 2003, the FAA’s Aviation Insurance Program has increased the federal government’s risk exposure “to as much as \$113 billion for 71 carriers” and the balance in the fund earmarked to pay potential claims “may not be sufficient to pay a carrier’s claim in a timely manner.” This raises the question of whether taxpayers would be on the hook if the fund is depleted after a major attack.



PENSION BAILOUT

As the airlines' economic situation worsened in the years following 9/11, several carriers that entered bankruptcy terminated their pension funds and transferred the responsibility to a federal agency, the Pension Benefit Guarantee Corporation (PBGC). TWA dumped its pension plans just prior to 9/11, and five others followed suit over the next several years: U.S. Airways, United, Delta, Aloha, and the U.S. branch of the Brazilian airline Varig. All told, responsibility for 16 pension plans covering nearly 240,000 employees fell to the PBGC. The assumption of this obligation was one of the major factors in a crisis that threatened to drain this federal agency's resources and raised concerns about the need for a tax-payer bailout.

Airline Defaults a Major Factor in Massive Deficits at Federal Pension Agency

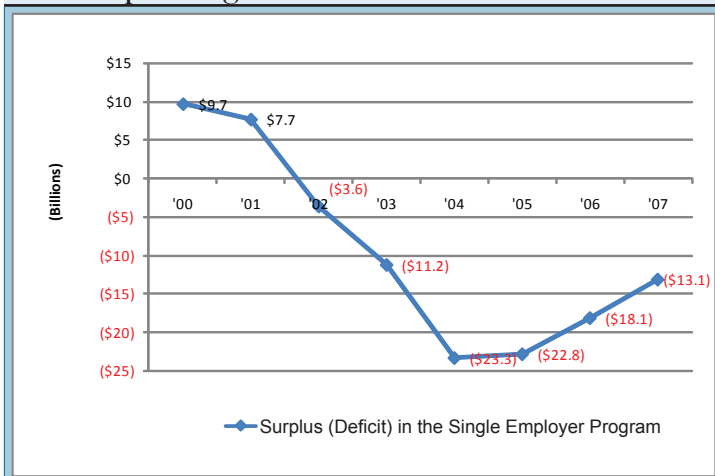
In the early- to mid-2000s, the PBGC appeared to be heading into crisis. The agency's Single Employer Program assumed responsibility for the airlines' pensions and represents more than 95 percent of the agency's balance sheet.⁵³ This program's financial condition plunged from a \$7.7 billion surplus to a \$3.6 billion deficit in the span of a single year.⁵⁴ By 2004, the deficit had risen to \$23.3 billion. In 2003, the Government Accountability Office placed the PBGC on its "high risk list"—a list intended to specify "agencies or major programs that need urgent attention and transformation to ensure that our national government functions in the most economical, efficient and effective manner possible."⁵⁵ It remains on that list to this day.⁵⁶

The Pension Benefit Guarantee Corporation

The PBGC is a federal corporation that was created in 1974 to act as a safety net for the nation's private-sector defined benefit pension plans. The protection it offers is basically a form of insurance: solvent companies pay regular premiums to the PBGC and the agency assumes responsibility for the pension plans of those companies that declare bankruptcy.

The PBGC is not funded by general tax revenues nor is it backed by the full faith and credit of the federal government. It is funded by employer premiums, investment income, assets from the pension plans it acquires, and recoveries from companies formerly responsible for the plans.⁵¹ Should an excessive number of claims deplete the agency's resources, however, the taxpayer could be obliged to step in. As David M. Walker, U.S. Comptroller General, testified before the Senate Committee on Commerce, Science, and Transportation in 2004: "Continued takeovers of severely underfunded plans make the eventual bankruptcy of PBGC an increasingly likely scenario."⁵² Congress would likely face enormous pressure to bail out the PBGC at taxpayer expense, according to Walker.

Figure 2-1: The PBGC Has Yet to Recover from Spiraling Deficits



Note: PBGC's Single-Employer Program, which covers airline and other employees, represents nearly all of the PBGC's assets and liabilities.

Source: Pension Benefit Guaranty Corporation

The principle reason for the PBGC's downturn was a sharp rise in annual net claims, coming primarily from the airline and steel industries. As of 2005—prior to the Delta and Aloha defaults—the airline industry accounted for 38 percent of all PBGC claims, despite paying only 2.6 percent of the premiums collected by the agency.⁵⁷ The United claim, filed in 2005, was the largest in the agency's history, at \$6.6 billion.⁵⁸

According to a 2003 GAO report, “The termination of large underfunded pension plans of bankrupt firms in troubled industries like steel or airlines was the major cause of the [PBGC’s] deficit.” United Airlines’ 2005 bailout was the largest in the agency’s history, at \$6.6 billion.

As the 2003 GAO report stated: “The termination of large underfunded pension plans of bankrupt firms in troubled industries like steel or airlines was the major cause of the deficit.”⁵⁹ A Congressional Research Service report issued in 2007 echoed this judgment.⁶⁰

Major Carriers Underfund Employee Pension Plans

As of 2004, according to the GAO, the pension plans maintained by the legacy airlines were underfunded by a total of around \$31 billion.⁶¹ The PBGC calculated that the 16 plans it has assumed responsibility for since 2001 were underfunded by more than \$21 billion at the time they were transferred.⁶² Due to statutory limits on the benefits the PBGC is required to provide, the obligation the agency assumed was less than \$21 billion.

The airlines were able to fall so far behind in their contributions, according to Bradley Belt, Executive Director of the PBGC at the time, because of weak federal regulation of pension funds.⁶³ The airlines were able to overvalue their pension funds' assets and undervalue their liabilities, thereby legally avoiding pension fund payments needed to keep the plans solvent.⁶⁴ As Belt explained, airline pension underfunding and the resulting PBGC deficits require fiscally responsible companies to subsidize those that default by paying higher premiums to the agency. The federal Deficit Reduction Act of 2005 increased the rate applying to most PBGC-insured employers from \$19 per participant to \$30.⁶⁵

Table 2-3: Underfunded Airline Pension Plans Transferred to the PBGC

Airline	Year	Number of Plans	Number of Participants
United Airlines	2004 and 2005	4	121,500
US Airways	2003 and 2005	4	63,000
Delta	2006	1	13,000
TWA	2001	2	36,500
Aloha	2006	3	3,900
Varig	2007	2	800
TOTAL:		16	238,700

Source: Pension Benefit Guaranty Corporation

Pension Reform Legislation Grants Subsidies to Airlines

The pension reform legislation that followed the PBGC’s downturn, while tightening many of these loopholes, also singled out the airline industry for substantial relief from funding requirements. This relief was accomplished by several laws, none of which involved an expenditure of government funds. The Pension Funding Equity Act of 2004 allowed airline and steel companies to defer up to

According to estimates by the PBGC and the *New York Times*, federal pension reform legislation in 2004 and 2007 saved the airlines more than \$3 billion.

80 percent of their deficit reduction contribution. According to Belt, six major airlines opted for this relief, resulting in \$1.3 billion less in contributions than would have otherwise been required over the course of 2004 and 2005.⁶⁶

The Pension Protection Act of 2006 gave airlines an extension on the period in which they are to bring the pensions to a fully funded status: 17 years, rather than the seven granted to most companies.⁶⁷ The act also allowed Northwest and Delta, both in bankruptcy at the time the act was passed, to freeze their pension plans and recalculate their obligations using a discount rate—8.85 percent—that would shrink those obligations considerably.⁶⁸ (Delta and Northwest’s discount rates the previous year had been 5.88 percent and 6 percent respectively.⁶⁹)

The following year, a pension measure tucked into an Iraq War spending bill offered similar relief to American, Continental, and a small number of regional carriers, allowing them to use a discount rate of 8.25 percent and reduce their payments to the funds over the next ten years.⁷⁰ The measure was intended to create a level playing field with Northwest and Delta. *The New York Times* estimated the value of the relief to American at \$2 billion.⁷¹

CHAPTER 3: SUBSIDIES TO THE AIRLINE INDUSTRY IN CALIFORNIA

- ▶ Since 2002, the airlines have received an estimated \$487 million in state and local subsidies in California, including tax exemptions and low-interest bond financing.
- ▶ Unlike motorists and other fuel users in California, airlines are exempt from state sales taxes on their purchases of jet fuel for some flights. The state Board of Equalization estimates that the airlines' fuel tax exemption for international flights will cost the state and local governments more than \$800 million over a five year period from fiscal year 2005 to 2009.
- ▶ The airline industry has lobbied repeatedly to expand this sales tax exemption to out-of-state domestic flights, which would cost taxpayers millions more.
- ▶ In 2002, United Airlines entered into an agreement with the City of Oakland that allowed the airline to avoid paying \$13.7 million in local jet fuel sales taxes over a four year period.
- ▶ Since 1970, airlines at LAX have received approximately \$1.3 billion in low-interest bond financing to construct or improve facilities or to purchase equipment. United Airlines has also received additional low-interest bond financing totaling \$412.8 million for improvements to facilities at LAX and SFO.

In addition to significant federal aid, airlines receive a variety of subsidies at the state and local level. Although not an exhaustive review, this chapter details some of the tax exemptions and low-cost financing that airlines have received in California.

Airlines Enjoy Sales Tax Exemption on Jet Fuel

Airlines pay significantly lower state taxes on fuel than the average motorist. Gasoline is taxed at \$0.18 per gallon, while jet fuel is taxed at only \$0.02 per gallon. Airlines, however, are excused from even this tax, because they are not included in the definition of "aircraft jet fuel users."⁷²

According to the State Assembly's *Revenue and Taxation Reference Book*, "In practice, the aircraft

jet fuel tax is imposed primarily on nonscheduled airline carriers (private jets and private mail delivery carriers) and helicopters."⁷³

On the state level, then, the primary tax burden on airlines for fuel comes in the form of sales and use tax, which ranges from 7.25 percent and 8.75 percent of a sale, depending on the local jurisdiction.⁷⁴ Since the early 1990's, however, airlines have been exempt from sales tax on jet fuel for any flight that has a foreign destination.⁷⁵ According to the California State Board of Equalization (BOE): "Sales of fuel and petroleum products are exempt from sales tax when sold for immediate consumption by an air common carrier on a flight whose final destination is a point outside the United States."⁷⁶

The exemption applies even if the air carrier makes multiple stops within the U.S. prior to the international stop. If a carrier’s final destination is Germany, for instance, the law would exempt the entire sale of fuel purchased in Los Angeles, even if that carrier had stops in San Francisco and New York en route.⁷⁷

The BOE estimates that this jet fuel exemption will cost the state and local governments more than \$800 million over the five year period from fiscal years 2005 to 2009, as shown in Table 3-1.⁷⁸ Both the BOE and the Legislative Analyst’s Office estimate the revenue loss to the state general fund to be \$104 million in the 2008/09 fiscal year.⁷⁹ The BOE’s total estimate also includes \$5 million that would have gone to the State Fiscal Recovery Fund and \$56 million to local entities, for a total loss to the state of \$165 million. In 2009-10, it projects this total will rise to \$170 million.

Prior to 1991, the jet fuel exemption applied to all out-of-state domestic flights, not only those with international destinations.⁸⁰ It also applied to water and rail common carriers. In July of 1991, the exemption was repealed due to the state’s budget

crisis. According to the BOE, repealing the exemption saved the state \$106 million in the first full year.⁸¹ As of 2005, the Air Transportation Association (ATA) estimated that losing the exemption had cost the industry more than \$400 million.⁸²

The industry has made frequent attempts to fight the 1991 repeal, proposing new legislation nearly every year since 1996. Nearly a dozen bills have been introduced into the California legislature since 1996 to expand the exemption again, either by restoring it for out-of-state domestic flights or exempting that portion of a sale above a certain dollar amount per gallon.⁸³ Most of these bills have been sponsored or supported by the ATA or individual airlines, including Southwest, Alaska, United, American, and Delta. None of the bills have passed. Their estimated annual cost to taxpayers has ranged from \$3.5 to more than \$140 million.

The second tax exemption the airlines enjoy in California is on aircraft and component part sales.⁸⁴ The BOE estimates a revenue loss of \$18.7 million annually for this exemption.⁸⁵ According to the BOE: “Sales of aircraft to common carriers,

Table 3-1: Estimated Revenue Loss from Fuel Tax Exemption

Revenue Loss (in millions)	2005-6	2006-7	2007-8	2008-9*	2009-10*	TOTAL
State General Fund	\$97	\$99	\$102	\$104	\$107	
Local	\$52	\$53	\$55	\$56	\$58	
State Fiscal Recovery Fund	\$5	\$5	\$5	\$5	\$5	
TOTAL:	\$154	\$157	\$162	\$165	\$170	\$808

* Projected

Source: California State Board of Equalization, *Tax Expenditure Report 2007-08*

to foreign governments for use outside California, and to nonresidents of this state who make no use of the aircraft in this state except to remove it, are exempt from tax.” In addition, the sale of component parts for aircraft maintenance and charges for labor and services related to maintenance are exempt from tax.⁸⁶

United’s Tax Rebate Deal with the City of Oakland

United Airlines further reduced its California sales tax payments on jet fuel purchases through an agreement with the City of Oakland that took advantage of loopholes in state tax law.⁸⁷ Jet fuel sales, like most other purchases in California, are subject to a state sales and use tax rate of 6.25 percent, the Bradley-Burns uniform local rate of one percent, and other optional local levies of up to 1.5 percent.⁸⁸ United was able to significantly reduce its payment of Bradley-Burns local taxes through its agreement with the city.

Since 1998, state law has required that the Bradley-Burns sales and use tax on jet fuel be allocated in one of two ways. If the seller has only one place of business in California, the tax is allocated at the point of sale—usually the sales office of the company. If the seller has more than one place of business in the state, however, the tax is allocated at the point of delivery to the aircraft—usually an airport. The intention was to redirect sales tax revenues away from the jurisdiction of fuel companies’ corporate offices and toward jurisdictions in which airports are located, to compensate for the services those jurisdictions provide for the airports.⁸⁹

In 2002, United Airlines entered into an agreement with the City of Oakland that made use of this law to divert 65 percent of the Bradley-Burns local sales tax revenue back to the company itself. United established a subsidiary known as a “single source purchasing and resale business” to purchase fuel for all United operations within California, thus establishing a single place of business at which all local sales taxes would be allocated. The company agreed to locate this business in Oakland, thus securing for the city sales tax revenues that would otherwise be distributed to other cities around the state, in exchange for a 65 percent cut of those revenues, to be issued as rebates, or “business incentive payments.”⁹⁰ In the four years that United’s agreement with Oakland was active, the city paid the airline a total of \$13.7 million, according to the Oakland Controller.⁹¹

San Mateo County filed a lawsuit against United, Oakland, and the Board of Equalization over the revenues it stood to lose under this agreement. This lawsuit claimed that the BOE changed the rule that allowed for this arrangement against the advice of its staff, after intense lobbying by several accounting firms, one of whom was at the same time working for United and shopping similar jet fuel deals around to various cities and counties.⁹²

Prior to this agreement, according to the Legislative Analyst’s Office, roughly half of the local sales tax revenues from United’s purchases were divided between San Mateo and San Francisco Counties, about 40 percent to the Los Angeles International Airport, and the remainder

to other areas around the state. The BOE estimated that the deal cost other local jurisdictions around the state \$9 million in lost tax revenues. The City of San Francisco estimated that it and the County of San Mateo stood to lose \$2.4 million and \$3.0 million annually. The City of Los Angeles estimated \$1.5 million.⁹³

In defending the arrangement, United claimed that it was reacting against rising fuel costs. “We feel that the deal was legal,” spokeswoman Megan McCarthy told the press. “We continue to focus on controlling our fuel costs.”⁹⁴ San Mateo County Deputy County Council David Silberman had a different take: “At its simplest, they intentionally redirected taxes to evade them. It doesn’t matter what your theories are, evading taxes is always wrong.”⁹⁵

In 2005, the state legislature approved a bill

According to San Mateo County Deputy County Council David Silberman, “At its simplest, they [United] intentionally redirected taxes to evade them. It doesn’t matter what your theories are, evading taxes is always wrong.”

authored by Leland Yee to close the loophole and prevent similar deals, AB 451. The bill went into effect January 1, 2008. It specified that all jet fuel sales after this date will once again be allocated to the point of delivery, not the point of sale, regardless of how many locations the retailer has in the state.

In June of 2006, Oakland entered into negotiation

with Jet Blue Airlines to create a similar arrangement, though with a slightly lower rebate ratio (60/40 instead of 65/35).⁹⁶ That contract, however, was never finalized.⁹⁷ The lawsuit that San Mateo County filed against Oakland and United in 2006 claimed that several other airlines, including Northwest, American, and Southwest, approached other municipalities in the Bay Area, looking to cut similar deals.⁹⁸ The San Jose City Council rejected one such deal with American in January 2006.⁹⁹

Airlines Benefit from Tax-Exempt Bonds at LAX

Due to its close relationships with publicly-owned airports, the airline industry has benefited from billions of dollars worth of tax-exempt bond financing around the country.¹⁰⁰ Although documenting the full extent of this financing is beyond the scope of this report, we include some information relating to bond financing in California.

Airlines in California have received at least \$1.7 billion in low-cost financing for improvements to their facilities at certain airports, thanks to tax-exempt bonds issued on the airlines’ behalf by non-profit and public entities like the Regional Airports Improvement Corporation (RAIC) and the California Statewide Communities Development Authority (CSCDA). Tax-exempt bonds represent a subsidy to the airlines because the interest rate is lower—and the cost of financing is less—than what they would receive in the private market. Because the proceeds from the bonds are tax-exempt, investors are willing to receive a lower rate of return

than they would otherwise. The cost to the taxpayer is the foregone tax revenue that the bond investors would have paid on the interest earned on their investment. Because the public cost of the bonds derives from foregone tax revenue, the taxpayer subsidy does not appear in state or local budgets.

RAIC is a non-profit corporation that was established in 1969 in order to “assist the city of Los Angeles by financing or otherwise, in acquiring, constructing, replacing, extending, enlarging, or improving airports, heliports, and the facilities thereof,” according to its IRS Form 990.¹⁰¹ Though RAIC does not receive public financing, its activities are subject to the approval of the City Council and the city’s Department of Airports.

Since the agency’s inception, RAIC has issued approximately \$1.3 billion in bonds, all of which

were used by airlines to construct or improve facilities or purchase equipment at LAX.¹⁰²

Eighteen airlines and related entities have received RAIC bonds financing, and the ten largest airline beneficiaries are listed in Table 3-2.

Since 1970, airlines at LAX have received approximately \$1.3 billion in low-interest, tax exempt bond financing to construct or improve facilities or to purchase equipment.

In addition to receiving financing at below-market rates, certain airlines at LAX also have long-term leases that give them a high degree of control over how the terminals are used. LAX is unusual among airports in that it only operates three and a half of its nine terminals. The rest are controlled

Table 3-2: The Ten Largest Recipients of RAIC Bonds at LAX

Issue	Date and Use of Funds	Total (In Millions)
American Airlines	Terminal Facilities, Hangar and Flight Kitchen Facilities (1971), Terminal Facilities (1984)	\$377.1
LAXFUEL Corporation	Fuel Systems Facilities (1991, 1994, 2001, 2005)	\$250.0
Delta Airlines	Terminal Facilities (1996), Maintenance and Employee Parking Facilities (1975), Terminal Facilities (1985)	\$193.9
United Airlines	Terminal Facilities (1982, 1984, 1992)	\$135.1
LAX Two Corp.	Terminal Facilities (1985, 1989)	\$111.9
Continental Airlines	Cargo Facilities (1994), Terminal Facilities (1988 and 1999)	\$92.3
Trans World Airlines	Maintenance, Cargo, and Terminal Facilities (1971 and 1973)	\$55.0
Korean Airlines	Cargo Facilities (1981, 1985, 1991)	\$32.4
Federal Express	Cargo Facilities (1979 and 1981)	\$17.5
LAXTEC Corp.	Terminal Equipment (1983)	\$16.8

Source: LAANE analysis of Los Angeles World Airports data

by carriers such as United, American, Delta and Continental, through long-term leases that give them the right to allocate gates.¹⁰³ Airport officials and industry analysts charge that some of these carriers underutilize their gates, which could be used by other airlines wanting to expand.¹⁰⁴ If this allegation is true, it could provide a competitive advantage to these airlines at LAX. Airlines in Terminal Two, at least, have denied the allegation, saying it would be impossible to increase flight capacity in that terminal.¹⁰⁵

established in 1988, is a statewide joint powers authority that is sponsored by the California State Association of Counties and the League of California Cities. Its purpose is “to provide local governments and private entities access to low-cost, tax-exempt financing for projects that provide a tangible public benefit, contribute to social and economic growth and improve the overall quality of life in local communities throughout California,” according to its website.¹⁰⁷ Like RAIC, it receives no public funding but relies on fees charged to private applicants.

United Secures Additional Bond Financing

United Airlines has also received bond financing totaling \$412.8 from the CSCDA.¹⁰⁶ The CSCDA,

Table 3-3: Tax-Exempt Bonds Issued to United Airlines by the CSCDA

Airport	Facilities	Date	Amount (in millions)
SFO	Passenger, cargo and related facilities	1997	\$154.8
LAX	Passenger and related facilities	1997	\$190.2
SFO	Gate modifications, renovations, repairs and installation	2000	\$33.2
LAX	Cargo handling and warehousing facility	2001	\$34.6
TOTAL:			\$412.8

Source: California Statewide Communities Development Authority



CHAPTER 4: POOR JOB QUALITY FOR CONTRACTED AIRLINE SERVICE WORKERS

- ▶ Historically a source of middle class jobs, the airlines have severely eroded job quality in the industry by outsourcing jobs and extracting major concessions from their in-house employees after 9/11.
- ▶ According to the *Wall Street Journal*, a growing number of airline jobs are similar to those in the fast food industry.
- ▶ A job quality analysis of 5,000 contracted airline service workers at four major airports in California found that their wages fall below self-sufficiency standards and health benefits are largely unavailable or unaffordable. Conditions are likely to be the same for the estimated 18,000 contracted airline service workers at airports throughout California.
- ▶ California taxpayers bear the cost when low-wage uninsured workers rely on government assistance programs and overtaxed public health care facilities and hospital emergency rooms.
- ▶ In Los Angeles, airline service jobs contribute to poverty in many of the communities most affected by pollution and noise impacts from LAX.

The airline industry has historically been a major source of middle class jobs, often attracting multiple generations of the same family.¹⁰⁸ Highly skilled—and heavily unionized—pilots, flight attendants, and mechanics have been able to count on decent pay and generous health and pension benefits. However, in recent decades, the quality of jobs available to workers in the industry has eroded, affecting lower-paid ramp and service workers as well as more highly compensated pilots and flight attendants. The airlines have employed two strategies to reduce labor costs.

First, they have reduced staffing and extracted wage and benefit concessions from their direct employees, often through bankruptcy

procedures.¹⁰⁹ According to the *Wall Street Journal*, airlines have cut wages and benefits so much that “a growing number of airline jobs are more akin to those at a fast-food restaurant,” leading to problems with recruitment and retention of employees. But even those at the higher end of the pay scale have seen the quality of their jobs erode. “An airline career is not worth it anymore,” a 23-year veteran pilot told the *Wall Street Journal*. Capt. Gene Malone had seen his annual pay drop by 20 percent and been forced fly more “red eye” flights from his base in Los Angeles. Andy Roberts, executive vice president for operations for Northwest Airlines Corp., said the major carriers used to have long lists of applicants, but now “we have to go seek them out, even pilots.”

As discussed in Chapter 2, the major carriers severely under-funded employee pension plans, and shifted the responsibility for pensions to the Pension Benefit Guarantee Corporation (PBCG), a federal corporation. Due to a Congress-mandated cap on benefit payments, many workers and retirees receive considerably less from the PBGC than they were originally promised by their employer.¹¹⁰ Pilots, flight attendants, and other relatively high paid employees are especially hard hit, often receiving a fraction of what they had been expecting. In the case of Aloha Airlines, for instance, 58 percent of the pilots saw an average 42 percent reduction in benefits, or around \$1,050 a month.¹¹¹

A second strategy employed by the airlines has been to outsource work. By contracting out service work to the lowest bidder, the airlines have created a class of low-wage jobs with minimal benefits that leave many workers eligible for publicly-funded anti-poverty programs. In essence, the industry is doubly subsidized: once through direct airline subsidies and again through workers' reliance on government assistance programs and public health care facilities.

In essence, the industry is doubly subsidized: once through direct airline subsidies and again through workers' reliance on government assistance programs and public health care facilities.

This chapter contains an analysis of job quality for 5,000 contracted airline service workers at four major California airports—Los Angeles International (LAX), San Francisco International (SFO), San Jose International, and Oakland International. These workers are employed by airline contractors and perform a range of key duties, including security, providing assistance to passengers with disabilities, baggage handling, and airplane cabin cleaning. At LAX and San Jose, findings are based on original worker surveys which were first released in reports by LAANE and Working Partnerships USA in 2007 and 2008, respectively.¹¹² The LAX survey was conducted by LAANE in March and April of 2007. Given the airlines' contracting policies that drive down wages and benefits, conditions are likely to be the same for the estimated 18,000 contracted airline service workers at airports throughout the state.¹¹³

Low Wages for Contracted Airline Service Workers in California

Local governments in Los Angeles, San Francisco, Oakland and San Jose have attempted to address the poor quality of airline service jobs through local living wage ordinances. However, airline service workers at all four airports do not earn enough to afford the high costs of living in Los Angeles and the Bay Area. In Los Angeles, San Francisco and Oakland, workers are covered by the living wage, but still do not earn enough to meet the basic needs of a typical family. In San Jose, airline contracted service workers are not covered by the city's living wage policy.

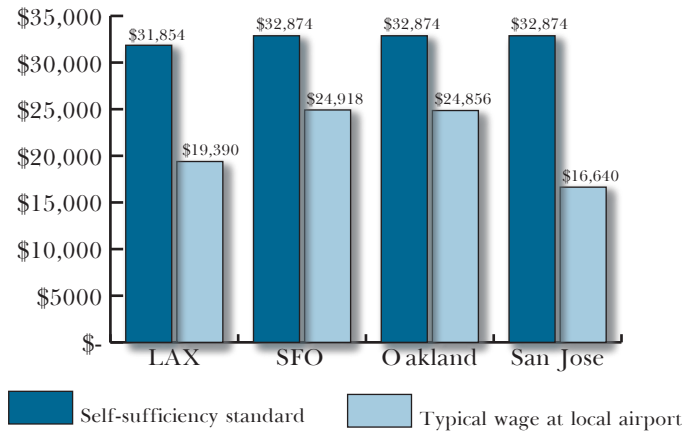


“I have been working as a Security Exit Guard at SFO for 10 years. We serve United Airlines

passengers. At 70 years old I would like to be able to retire but I cannot afford to. I can’t stop working because I need money to support my medical condition. I’m diabetic and have hypertension. I pay \$94 every paycheck for my medical insurance. I feel like I am working just to pay my medical insurance.”

—Sonia Galan, Security Exit Guard for a United Airlines contractor at SFO

Figure 4-1: Earnings for Contracted Airline Service Workers at Major California Airports Fall Below Self-Sufficiency Standards



Sources: California Budget Project, 2007 LAANE LAX Survey, 2008 Working Partnerships San Jose Survey, SFO Collective Bargaining Agreements, Oakland Living Wage Ordinance, SEIU

As shown in Figure 4-1, surveyed workers at LAX earn only 61 percent of what they need to meet a self-sufficiency standard for L.A. County.¹¹⁴ Wages for workers at SFO and Oakland are at 76 percent of the self-sufficiency standard for the Bay Area. Workers at San Jose International Airport do the worst, earning only half of what they need to be self-sufficient because they are not covered by the city’s living wage policy.¹¹⁵ If they were covered by the living wage and working full-time, they would reach 88 percent of the self-sufficiency standard.

Specific wage standards at each airport vary. All the living wage policies include a two-tier wage,

which gives employers the choice of paying a higher wage, or a lower wage with a \$1.25 per hour contribution to health care benefits for the employee. LAX is the airport with the lowest living wage level, at \$11.25 per hour or \$10.00 per hour, while Oakland is higher, at \$12.45 or \$10.83 per hour. At SFO, the standard is \$13.13 or \$11.88 per hour. San Jose’s standard is the highest, at \$14.08 or \$12.83 per hour.

The self-sufficiency standard used in this report is based on the basic needs budgets calculated by the California Budget Project (CBP) for various regions in the state. The CBP calculates the cost in each region to meet the basic needs of different family types, which includes necessities like housing, food and child care, but not items like vacations or saving for college or retirement. A worker or family that earns enough to meet its basic needs

without having to rely on government assistance or charity can be considered self-sufficient. The self-sufficiency standard in this report is based on the basic needs budget for a family with two working parents and two children.¹¹⁶

Conditions at LAX illustrate the difficulties faced by low-wage airline service workers. Although LAX workers receive the living wage, their annual earnings are suppressed because many workers do not receive full-time hours. This makes it even harder for them to achieve a decent standard of living and forces many to work more than one job. LAX workers have also seen little improvement over the years. The LAANE survey found that even workers who have been with the company for 10 years are making just above living wage, despite years of experience.

Health Benefits are Unavailable or Unaffordable for Many Contracted Workers

Not only are wages low, but health benefits for many airline service workers are either unavailable or unaffordable.¹¹⁷ Although the living wage laws at the four airports include a \$1.25 per hour wage differential for companies that provide health benefits, this amount is not sufficient to pay for adequate health care coverage. The \$1.25 level has not been adjusted since the living wage laws were passed, while health plan premiums have increased greatly. In 2007, the average cost for employer-provided individual health benefits was \$2.00 per hour, while the cost to employers for family benefits was \$5.20 (assuming full-time work).¹¹⁸

Airline Service Worker Faces Homelessness



Dwayne Green, wheelchair agent for a Southwest Airlines contractor at San Jose International Airport.

Dwayne Green has worked at the San Jose International Airport as a wheelchair agent for two years and in the California airline industry for more than 39 years.

A few of Dwayne's co-workers who are contracted directly by the City of San Jose earn a living wage, but most of them earn only eight dollars an hour. The only raises he receives are when the state increases the minimum wage. Consequently, making ends meet is nearly impossible.

For almost a year, even while working full time at the airport, Green was homeless, sometimes living in local shelters and sometimes on the street. Unfortunately, the wages he received made it impossible to pay rent and provide food for his family.

Table 4-1: Health Benefits Are Unavailable or Unaffordable for Most Contracted Workers

Airport	Quality of Health Benefits
LAX	<ul style="list-style-type: none"> ➤ Nearly 70 percent of workers surveyed are not enrolled in an employer-provided health plan. The average cost to surveyed workers to obtain basic family coverage is \$250 per month. ➤ Workers are covered by the city’s Living Wage Ordinance, but it provides an insufficient amount for health care (\$1.25 per hour).
SFO	<ul style="list-style-type: none"> ➤ Individual coverage is provided for many workers, but is not affordable in all cases. ➤ Most workers are not currently covered by the city’s Health Care Accountability Ordinance, which provides a \$2.00 per hour health care credit. ➤ Family coverage is unavailable or unaffordable.
San Jose	<ul style="list-style-type: none"> ➤ Individual and family benefits are unavailable or unaffordable. ➤ Workers are not covered by the city’s Living Wage Policy.
Oakland	<ul style="list-style-type: none"> ➤ Individual and family benefits are unaffordable or unavailable. ➤ Workers are covered by the city’s Living Wage Ordinance, but it provides an insufficient amount for health care (\$1.25 per hour).

Source: LAANE’s 2007 LAX Survey, Working Partnerships USA’s 2008 San Jose Survey, SEIU

The \$1.25 per hour health care differential in local living wage policies has not been adjusted since these laws were passed.

At LAX, coverage is unavailable, unaffordable or not comprehensive for many contracted workers. World Service, a major contractor that employs 300 workers at LAX, does not offer a health plan at all. Workers who are offered coverage report that the plans provide limited levels of coverage or have high out-of-pocket costs. G-2 Secure Staff employees, for example, have a “limited accident and sickness insurance plan” which contains limits

on benefits, in addition to high premiums. Not surprisingly, only 32 percent of LAX workers surveyed enroll in the employer health plans for themselves.

While some workers at LAX can afford their share of employer-paid individual coverage, family coverage is out of reach. On average, workers would have to pay over \$3,000 a year for family benefits, and some company plans cost workers as much as \$5,000 annually. For low-wage workers struggling to afford basic necessities such as housing and childcare, this cost is nearly impossible to pay.



“I have worked as a skycap at San Francisco International Airport for nearly 18 years, providing service for American Airlines.

I love working with the public. I work hard to provide a decent life for me and my wife. But it’s hard when the cost of rent, gas, and food keeps going up. My wife has breast cancer and I pay close to \$400 a month for her healthcare costs. It’s not easy making ends meet in the Bay Area, but the airlines have made it nearly impossible.”

—Patrick Jack, Skycap for an American Airlines contractor at SFO

Conditions at SFO are better, but still far from adequate. Workers report that some contractors provide affordable individual health care coverage, but others do not. Family coverage is unavailable or unaffordable, leaving workers to rely on public health care facilities or public insurance programs for their children’s health needs. At San Jose and Oakland, workers report that both individual and family coverage are either unavailable or unaffordable. At San Jose, none of the workers surveyed reported having access to employer-provided healthcare.¹¹⁹

Taxpayers Bear the Costs of Poor Quality Jobs

The cost of poor quality jobs is borne by the public. More than half of all individuals using major government assistance programs in California are in working families. It is estimated that providing public programs such as Medi-Cal and Food Stamps to working families cost California taxpayers more than \$10 billion in 2002.¹²⁰ Uninsured children in low and moderate-income working families are also eligible for Healthy Families, a publicly-funded health plan.

Jobs that lack health benefits create public costs and place increasing strain on the county’s overburdened public hospitals and emergency rooms. Across the state, over 6.5 million people are uninsured, representing 20 percent of the non-elderly population.¹²¹ Nearly half of people without health coverage postpone seeking medical care.¹²² Moreover, costs that hospitals and doctors incur by caring for the uninsured translate into higher premium costs for those who do have insurance. This increased cost has been estimated at \$1,160 per year for family coverage.¹²³

It is estimated that providing public programs such as Medi-Cal and Food Stamps to working families throughout the state cost California taxpayers more than \$10 billion in 2002.

Surveyed LAX Workers More Likely to Be Minorities Who Live in Communities Most Affected by Airport Pollution

More than 60 percent of surveyed workers at LAX live in communities surrounding the airport or in South Los Angeles.¹²⁴ Workers also live

Surveyed workers at LAX live in high-poverty communities, such as South LA and Lennox.

in the high poverty communities of Compton, Lynwood and Southgate further east.¹²⁵ Among zip codes in which surveyed workers live, one in four families (26 percent) live below the federal poverty level,¹²⁶ nearly double the rate for the entire county (15 percent).¹²⁷ In addition, over 50 percent of households make less than \$35,000 a year. South Los Angeles, where many airline service workers live, has the highest numbers of uninsured children in the county and the second highest rate of uninsured adults.¹²⁸

Communities near airports and in their flight path disproportionately bear the cost of pollution and noise impacts from the airport. Studies have found higher rates of health problems in communities surrounding LAX. Between 1998 and 2000, the California Office of Statewide Health Planning and Development (CA OSHPD) ranked cases of asthma hospitalization across the state. Among the nine assembly districts

in which LAX surveyed workers live, six were in the ten with the highest rates of asthma hospitalizations.¹²⁹ Communities in the airport's flight path are adversely impacted by the noise from jet engines as well, which can be as loud as 94 decibels, a level which can cause hearing problems.¹³⁰ The LAX Master Plan Supplement Environmental Impact Study/Environmental Impact Report found that schools in the flight path were exposed to significant levels of exterior noise that caused disruptions in speech and elevated ambient noise levels believed to be disruptive to learning.¹³¹

“I live in a neighborhood in South LA that has a lot of poverty. A lot of my co-workers



live there too. It's hard to move up and improve our families and communities with the kind of jobs that are available at LAX. The airport should be doing more to make sure that jobs at LAX pay a good wage. It would make a big difference in my neighborhood.”

—Robin Wilson, Wheelchair Agent for an American Airlines contractor at LAX

The great majority of LAX and San Jose workers surveyed are people of color.¹³² More than two thirds of LAX workers surveyed are Latino, while over 20 percent are African American, which is double their percentage of the population county-wide.¹³³ In San Jose, 90 percent of workers surveyed are either Asian-American, Latino, or African-American. These groups make up 65 percent of San Jose’s overall population.¹³⁴

Table 4-2: Airline Service Workers Surveyed are Predominantly People of Color

Ethnicity	LAX	San Jose
Latino	65%	13%
Asian-American/PI	10%	65%
African-American	21%	13%
White	3%	6%
Other	1%	4%

Source: LAANE’s 2007 LAX Survey, Working Partnerships USA’s 2008 San Jose Survey

Airline Executive Pay Protected as Employees Suffer

Airline executives have been careful to protect the benefits of managers and executives, even as in-house employees have lost substantial portions of their pensions and outsourced workers lack any retirement plans.

United Airlines

United CEO Glenn Tilton joined the company in 2002 with a pay package that included a \$950,000 annual salary, a \$3 million signing bonus and a \$4.5 million retirement plan. When the company filed for bankruptcy and dumped its pensions later that year, he took a pay cut—around \$344,000 over the next few years—but retained the signing bonus and the retirement package.¹³⁵

When United emerged from bankruptcy in February 2006, it was with a management compensation plan that set aside 8 percent of outstanding shares in the reorganized company for 400 of its managers.¹³⁶ The top eight managers thus stood to receive \$45 million in shares, including \$15 million for Tilton, depending on how the company was valued once it emerged. Airline Pilots Association International president Captain John Prater, testifying before the House Judiciary Committee, estimated Tilton’s post-bankruptcy compensation at more than \$40 million. By comparison, he stated, the pilots underwent two pay cuts—first 30 percent, then an additional 12 percent—harsher work rules, decreased job security, and the termination of their pension plan, and emerged from bankruptcy with only a 1.5 percent raise and a form of profit sharing worth about 0.5 percent of their annual earnings.¹³⁷

US Airways

US Airways then-Chairman Stephen Wolf received a \$15 million retirement payment only months before the company filed for bankruptcy in 2003.¹³⁸ When the company returned to bankruptcy court again in 2005, it sought approval for a special retention and severance package for 25 company officers and 1,870 salaried workers, intending to preserve their pension plans while dumping those of the flight attendants and other employees. (It had already dumped the pilots' plan in 2003.) The judge, Stephen Mitchell, approved the plan for managers but not company officers, stating in his ruling: "There is something inherently unseemly in the effort to insulate the executives from the financial risks all stakeholders face in the bankruptcy process."¹³⁹

Judge Stephen Mitchell, who rejected US Airways' proposed retention and severance package for its company officers, stated in his ruling: "There is something inherently unseemly in the effort to insulate the executives from the financial risks all stakeholders face in the bankruptcy process."

Delta

Delta, similarly, arranged bankruptcy-proof pension plans for more than 30 executives in 2002. It later dismantled the program, but only after making \$45 million worth of trust payments that executives were allowed to retain.¹⁴⁰



CHAPTER 5: AIRLINE CONTRACTING POLICIES PUT SECURITY, SAFETY AND SERVICE QUALITY AT RISK

- ▶ Airlines have compromised security by failing to ensure adequate training for contracted workers with security duties, according to surveys at Los Angeles International Airport (LAX) and San Jose International Airport (SJC) conducted in April of 2007 and January of this year, respectively.
- ▶ The LAX survey found that airlines were not providing adequate services to the elderly and to passengers with disabilities because of equipment problems, lack of training, and understaffing.
- ▶ Workers at LAX also reported that public health has been threatened by inadequate cleaning of airplane cabins.

Results from surveys of workers employed at two major California airports show that airline contracting policies have not only eroded job quality, but have also driven down the quality of services provided to passengers and have compromised public safety.¹⁴¹ This chapter draws largely from two previously released reports containing the results of surveys of contracted airline service workers. *Building a Better Airport*, released by Working Partnerships USA in April of 2008, includes a survey of 48 airline service workers at San Jose Airport, including security agents, wheelchair attendants, baggage handlers, terminal support workers and skycaps. *Under the Radar*, released by LAANE in July of 2007, includes a survey of 275 contracted airline service workers at LAX, covering the same occupations with the addition of aircraft cabin cleaners.

Contracted airline service workers play a vital role in ensuring airport security and passenger safety. Some of their duties are directly related to security, including searching airplane cabins

for dangerous items, guarding access to secure areas of the airport and airplanes, crowd control, guarding planes, and staffing security checkpoints. Other duties have security-related effects, such as baggage porters who play a role in the baggage screening process. In addition, airline service workers are the airport's ambassadors to the traveling public, with responsibilities like assisting passengers in wheelchairs. Table 5-1 describes the duties of surveyed airline service workers. Some airlines also contract for ramp services, ground handling, and cargo services on the airfield, but these workers were not included in the surveys.

The surveys found that, despite the vital role they play in ensuring airport security and passenger safety, many airline service workers were poorly paid, under-trained, and ill-equipped to do quality work—and the airlines were failing to provide adequate staffing levels to ensure public safety and quality service. Meanwhile, airports exercise little oversight over airline contractors.

After LAANE published the survey of LAX workers, some improvements were made by some contractors there, such as the purchase of new wheelchairs and some employee training sessions. But as long as contractors are pressured to cut costs without maintaining adequate standards for service, these improvements are not likely to be comprehensive or long-lasting.

Los Angeles and San Jose airports are not alone in facing this challenge. The airlines have outsourced workers in airports across the country. In order to win bids, airline contractors face intense pressures to cut costs, resulting in lower wages and benefits, minimal training for employees, and poor equipment standards. A 2003 UC Berkeley study found that airline outsourcing “created a national race to the bottom in the wages and working conditions of pre-board security screeners and others fulfilling important airport security functions.”¹⁴² A General Accounting Office (GAO) report found screener performance was impaired by lack of training and high turnover rates, which posed significant risks for airport security.¹⁴³

After the 9/11 attacks, screeners became employees of the federal Transportation Security Administration (TSA), in an effort to improve security by increasing training, improving compensation, and reducing employee turnover. But many important security functions remain in the hands of private security contractors.

Lack of Training Compromises Security

The surveys of airline service workers at Los Angeles International Airport (LAX) and San Jose International Airport (SJC) found a disturbing pattern of inadequate training for employees with security-related duties.¹⁴⁴ The vast majority of workers with security-related duties at LAX and SJC said they had no formal training on how to evacuate a terminal or how to identify suspicious behavior. In addition, 88 percent of LAX surveyed airline service workers had no formal training on emergency procedures, while only about half of surveyed SJC airline service workers had such training. (See Table 5-2.)

Table 5-1: Surveyed Airline Service Workers Have Crucial Security, Customer Service and Public Health Functions

Security Duties	Check airplanes for suspicious or dangerous items. Staff security checkpoints, and provide crowd control. Control access to airport areas and guard airplanes.
Porter and Sky Cap Duties	Transport baggage for passengers upon arrival at the terminal. Load and unload screened baggage from aircraft.
Wheelchair Attendant Duties	Assist elderly passengers and passengers with disabilities. Lift and assist passengers in and out of wheelchairs, escort passengers through customs and immigration, retrieve baggage and make sure passengers are met by their parties.
Janitorial Duties	Clean airplanes including changing pillows and blankets, vacuuming aircraft, and removing trash. Clean lavatories. Restock galleys. Clean terminals including floors and restrooms.

Source: LAANE's 2007 LAX Survey

Table 5-2: Emergency Response Training Received by Security Workers

	LAX	SJC
No formal training on how to evacuate a terminal	91%	80%
No formal training on procedures in an emergency	88%	48%
No formal training on identifying suspicious behavior	75%	64%

Source: LAANE's 2007 LAX Survey, Working Partnerships USA's 2008 San Jose Survey

In addition, 77 percent of LAX workers with security responsibilities reported that they had not been formally trained on how to properly conduct a plane search for suspicious items or procedures to follow if an item is found. LAX workers reported having as little as 15 minutes

“Part of my job is to check planes for things like weapons, dangerous items or contraband. My training consisted of watching a 20 minute video and taking a quiz. One of our biggest problems is having enough time to do the job. When there’s a delay of any kind, the airline staff put a lot of pressure on us to speed up our search, and sometimes it’s hard to search thoroughly.”

—Shea Smith, customer service agent for an American Airlines contractor

to conduct these searches. Inadequate training for these employees could create serious risks to airport security. Some airports, such as Miami International Airport and Boston’s Logan International Airport, have recognized the importance of training all airport workers in identifying potentially dangerous individuals by their behavior patterns, and have adopted such a training program for all airport staff, including airline service workers.¹⁴⁵

Adequate staffing is also a key to keeping California’s airports safe. Some passengers insist on accessing their luggage after it has been screened, which is a violation of TSA procedures. According to the LAX survey, 36 percent of baggage handlers reported that they were not always able to re-screen baggage after was opened by passengers, resulting in increased dangers to passengers and the community.

Low worker retention rates compound the problem of inadequate training and staffing. At SJC, only 10 percent of the workers surveyed had been employed at the airport for more than two years. Nearly one third of the workers surveyed had worked at the airport for less than 12 months. The LAX survey found that 25 percent of surveyed workers had been at their jobs for less than a year and more than 50 percent had been there for three years or less. Ultimately, improvements in worker training will largely be wasted if employees leave for better jobs.

Substandard Service for Travelers with Disabilities and the Elderly

Airlines and their contractors are required to provide adequate training to staff interacting with passengers with disabilities in order to comply with the 1986 Air Carrier Access Act. After several airlines were penalized for failing to meet federal standards, some took steps to improve services to disabled passengers. However, recent Department of Transportation reports reveal that problems continue. In the three years that federal statistics have been made available, more than 34,000 disabled flyers have complained about poor treatment, and more than 54 percent of the reported incidents have involved wheelchair assistance.¹⁴⁶

Surveys of LAX wheelchair attendants revealed that they were ill-equipped to provide quality service, and that airline service contractors were not providing the appropriate staffing and training. In fact, nearly a third of all surveyed wheelchair attendants at LAX said they have had a passenger in a dangerous situation as a result

Three-quarters of LAX wheelchair attendants reported working with broken or malfunctioning wheelchairs. Poorly maintained wheelchair equipment threatens the safety of passengers with disabilities and workers who assist them.

of poor training or equipment.

Three quarters of LAX wheelchair attendants reported working with broken or malfunctioning wheelchairs. Poorly maintained wheelchair equipment threatens the safety of passengers with disabilities and workers who assist them. Furthermore, it is likely to be a violation of federal regulations, which requires airlines to have procedures for the “proper and safe operation of any equipment used to accommodate individuals with a disability.”¹⁴⁷

In addition, 40 percent of all LAX wheelchair attendants surveyed indicated that they have been responsible for more than one passenger at a time because of short staffing. Often this meant passengers endured long waits for assistance or attendants were forced to travel back and forth between two passengers. Sixty-three percent of LAX wheelchair attendants surveyed had no formal training on how to lift a traveler with a disability, risking the health of passengers and workers alike. In addition, only six percent of LAX attendants reported receiving training on how to administer first aid or CPR, despite working with a population likely to need these basic medical services. Although all San Jose wheel chair attendants report receiving training on lifting passengers, only seven percent had training in CPR and first aid.

Service Quality Undermined

As contractors lower costs to compete for airline contracts, the quality of the services these companies provide suffers. For passengers, that can mean longer lines, lost bags and dirty cabins. Airlines have allowed service quality to decline despite a 2006 report by J.D. Power and Associates that found that carriers that focus on people and processes have greater passenger satisfaction. The J.D. Powers report stresses that having the right workers and “training and enabling them to be successful, are what differentiate carriers in the eyes of passengers.”¹⁴⁸ Yet half of LAX workers reported that they could not provide high quality work because of insufficient staff, and half of LAX workers said they did not have the proper equipment to provide quality services to passengers.

“We are often short-staffed on certain flights. We’ve been told that’s because the airline’s not paying for full staffing. Short-staffing means that if we have a passenger with rolling luggage, we end up pushing the wheelchair with one hand, and pulling the bag with the other. This makes it hard to control the wheelchair and is dangerous for the passengers and us.”



—Carolina Franco, Wheelchair Agent for a Northwest Airlines contractor at LAX



One third of surveyed cabin cleaners at LAX said they did not have enough time or staff to change all the pillowcases and blankets on planes between flights. As a result, passengers may be coming into contact with used items that could spread germs or disease.

Inadequate staffing can have security implications, as discussed above. It can also impact public health. One third of surveyed cabin cleaners at LAX said they didn't have enough time or staff to change all the pillowcases and blankets on planes between flights. As a result, passengers may be coming into contact with used items that could spread germs or disease.

In addition, a third of surveyed porters and skycaps at LAX said that passengers have received the wrong bags. The problem of lost bags is not unique to LAX. In February 2008, 6.39 out

“Improving training doesn't really help if the trained people don't stay. Many of my co-workers have left for better jobs, so we have a lot of new people who don't have much training or experience.”



—Paula Lopez, Wheelchair Agent for an LAX contractor hired by international airlines like Mexicana and Qantas

of every 1,000 passengers on domestic flights filed a mishandled baggage complaint with the Department of Transportation, an increase from 4.39 in October 1998.¹⁴⁹



CHAPTER 6: CONCLUSION AND RECOMMENDATIONS

This report has documented an estimated \$8.5 billion in taxpayer subsidies to the airline industry at the federal, state, and local levels. In reaction to the severe financial impact of the 9/11 attacks on the industry, the federal government provided massive aid through a variety of programs. The devastating effect of 9/11 on the industry cannot be denied. But when passenger traffic returned to pre-9/11 levels and the airlines reported profits, they continued to benefit from several key subsidies initiated after 9/11.

At the state and local levels, airlines also receive significant subsidies, and California is a case in point. Compared to the average private motorist in the state, airlines bear a much lighter sales tax burden for fuel, and have made numerous attempts to decrease their taxes even further. Airlines have also benefited from more than \$1 billion in below-market rate bond financing at California's two largest airports, LAX and SFO, since 1970.

While the industry recovered financially from 9/11 in 2006, it now faces another financial crisis brought on by escalating oil prices. So far this year, several airlines have filed for bankruptcy and industry merger talks have begun. Now more than ever, it is important to ensure that subsidies to the industry result in significant benefits to the public, in the form of good jobs, passenger safety, and quality service. Though the financial challenges currently faced by the industry are serious, they should not

be a justification for further erosion of job quality, safety and service standards. Instead, the industry should recognize that investing in its workforce and improving service quality are essential steps towards its long-term success and profitability.

The airlines may argue that subsidies are justified because they make air travel affordable to a broad segment of the population and that they are a linchpin of the nation's economy. However, an industry's contribution to the economy should also be measured by the ability of its employees to sustain their families, obtain health care, and participate in the consumer economy. By these measures, the airlines fall far short. The quality of jobs provided by the airline industry has been severely eroded both by outsourcing and by cuts in compensation for in-house employees since 9/11.

Instead of providing middle-class jobs that enable employees to provide for their families and retire in dignity, “a growing number of airline jobs are more akin to those at a fast-food restaurant,” according to the *Wall Street Journal*. Contracted employees fare even worse.

Instead of providing middle-class jobs that enable employees to provide for their families and retire in dignity, “a growing number of airline jobs are more akin to those at a fast-food restaurant,” according to the *Wall Street*

Journal.¹⁵⁰ Contracted employee fare even worse, with wages falling below self-sufficiency standards and minimal benefits provided to many airline service workers at the four major California airports examined in this report. Taxpayers foot the bill twice, once for the initial subsidy and again when low-wage, uninsured workers rely on government assistance programs.

While air travel is now more affordable than in the regulated era, airline service quality ratings have fallen to their lowest level in nearly two decades.¹⁵¹ Cost-cutting and contracting out of key services have raised serious concerns about aircraft maintenance, security and public safety. Worker surveys at LAX and San Jose airports have revealed an undertrained, unstable

contracted workforce that is responsible for providing critical security and passenger services. All told, the airlines have failed to live up to their responsibility to adequately protect and provide quality services to passengers.

Fortunately, efforts are underway to improve conditions in this industry. At four of California's major airports—LAX, SFO, San Jose, and Oakland—contracted service workers are joining with community groups, disability advocates, clergy, and elected officials to raise job quality, training and service standards. In order for the airline industry to truly provide a return on the public's investment, both the airlines and the public sector have a role to play.



Recommendations

1. **The airline industry should provide a fair return on the public's investment by creating middle-class jobs and ensuring quality service and passenger safety.**

The airline industry should provide jobs with adequate wages, benefits and training to both its contracted and in-house employees. The airlines should not view their current financial challenges as a justification for low-wage jobs without health benefits and declining safety and service quality. Instead, the industry should recognize that its long-term success and profitability depend in part on a stable, trained workforce and that airlines can become more competitive by providing superior service to passengers.

Studies have shown that improving pay and benefits for low-wage workers lowers employee turnover and improves productivity.¹⁵²

“As our airline research has shown, a high level of engagement and a good labor-relations system are the keys to increasing productivity and service quality. And productivity leads to profitability.”

—Tom Kochan, Professor of Management at MIT, as quoted in the *Wall Street Journal*

According to MIT Professor Tom Kochan's research on the airline industry, improving employee compensation and labor relations will ultimately lead to higher productivity and more profitability.¹⁵³ He concludes that in a cost-driven industry such as this one, cutting labor costs to the bone may save money in the short run, but leads to productivity losses and lower profits in the long run.

Improvements in employee training and retention will pay off in improved service quality, safety, and security. A report released this year by J.D. Power and Associates found that customer satisfaction with the airline industry is at its lowest level in three years, and this decline is largely driven by deteriorating levels of customer service provided by employees. The study concludes that, “In this unstable industry environment, it is critical that airlines invest in their employees as a means to enhance the customer experience, as there is a strong connection between employee satisfaction and customer satisfaction. Those airlines that focus on keeping their employees informed and motivated will be better able to change negative consumer sentiment and truly differentiate themselves.”¹⁵⁴

2. Federal, state, and local officials should take action to raise standards for job quality, security and service quality in this industry.

Policy initiatives are currently underway at many of the airports discussed in this report. LAX officials recently approved a Service Standards Policy to improve airline contractor performance and ensure that only the most qualified contractors are allowed to operate there. Detailed quality standards have not been developed yet, and city officials should use this opportunity to re-evaluate the effectiveness of the existing living wage standard. The Los Angeles living wage is the lowest of the four airports examined in this report, and falls the farthest short compared to local costs of living.

In San Jose, the City Council is considering expanding its living wage policy and other job quality standards to cover all employers and airline contractors at the airport. This action is to be commended, and will represent significant progress towards bringing compensation for airline service workers more in line with the local cost of living.

Since 2000, SFO has had a Quality Standards Program in place for airlines and their contractors which sets standards for wages, hiring, safety training, safety procedures and the disclosure of security training practices. Airline contractors, however, are not consistently covered under two additional airport policies

that set job standards—the Minimum Compensation Ordinance, which requires employers to provide 12 paid days off and the Health Care Accountability Ordinance, which requires employers to provide a health benefits plan or to pay the city a \$2 per hour per worker fee to support the city’s public health facilities. SFO is currently reviewing the application of these three policies with a goal of developing a consistent standard that improves conditions for airline contracted workers.

At both the state and federal levels, efforts have been made to institute an airline Passenger Bill of Rights. In California, State Assemblymember Ted Lieu has introduced AB 1407, which would require airlines to ensure that passengers receive adequate care when they are on board a delayed flight and increase the amount of compensation airlines are required to provide to passengers if they miss a connection due to a delayed flight. The bill would also create an Office of the Airline Advocate, which would investigate and resolve consumer complaints against the airlines. Assemblymember Mark Leno has also introduced a similar bill, AB 1943, which protects passengers by requiring airlines to provide basic amenities such as food, water, lights, air, and working toilets if a plane is delayed on the tarmac. In Congress, bills to create a Passenger Bill of Rights were introduced in both the Senate and the House in 2007, but never came to a vote.

3. Government programs that provide subsidies to business should contain public benefit requirements.

Poor conditions in the airline industry are partly due to the fact that generous public subsidies to the industry came with few strings attached. A rare exception is the post-9/11 loan guarantee program, which required airlines to freeze the salary of executives making over \$300,000 for the two years following 9/11. This and other public benefit requirements relating to job quality and service quality should be attached to subsidies at the federal, state and local levels.

Even further, as Professor Kochan points out, the public sector makes decisions that provide

economic benefit to the airlines on a frequent basis, and those decisions create opportunities to improve conditions for employees. The federal government may soon be considering decisions that provide the leverage to force change. As Kochan states, “It [the federal government] can hold up mergers until the companies show that they’ve got a business plan to address these issues.”¹⁵⁵ The airline industry is also advocating changes to the system of taxes and fees that fund FAA operations that would result in corporate aviation users paying a greater share.¹⁵⁶ The federal government should use its role in these decisions to ensure that the airline industry contributes to the economy by providing middle-class jobs while maintaining high standards of security, safety, and service for the traveling public.



ENDNOTES

¹ “Executive Briefing: A New Approach for Airlines,” *Wall Street Journal*, May 12, 2008, p. R3.

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¹¹⁴ At the time the LAX Job Quality Survey was conducted in spring of 2007, the average earnings of surveyed workers were \$18,824. Since that time, the Living Wage Ordinance (LWO) level has increased by three percent, so we adjusted the average reported earnings upwards by

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APPENDIX A

Major Airlines and Airline Service Contractors at Four California Airports		
Airport	Major Airlines and Percent of Total Airport Passenger Traffic*	Major Contractors
LAX	American (20%) United (18%) Southwest (16%) International airlines, such as Qantas and Mexicana	G2 Secure Staff Air Serv Corp Aviation Safeguards Aero Port Services Calop Aviation World Service West One Source Menzies Swissport Evergreen ASIG
SFO	United (41%) American (13%) Sky West (9%) Delta (6%)	Primeflight G2 Secure Staff Air Serv Corp Prospect Aviation Covenant Aviation Security Menzies Swissport ASIG
OAK	Southwest (64%) JetBlue (8%) Alaska (8%)	Aviation Safeguards DAL Global Services Air Serv Corp Windjammers
SJC	Southwest (45%) American (10%) Alaska (7%) United (7%)	Aviation Safeguards G2 Secure Staff

* from 4/07 to 3/08

Sources: U.S. Dept. of Transportation, Bureau of Transportation Statistics, LAWA, SEIU