

**Submission
to the
House of Commons
Standing Committee on Transport**

on

**Air Liberalization
and
Canadian Airports System**

Submitted by

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Executive Summary

The aviation system is a pillar of our national social and economic development. Manitoba has a need for efficient air services and air infrastructure to support business access to markets, tourism, as well as the needs of our isolated citizens in remote communities.

Manitoba asserts that the aviation policy framework be based on the following principles:

- The primary objectives of the system should be to serve the needs of travellers and shippers, and to maintain the economic well-being of Canada and its regions;
- Competition in the air industry is the best mechanism to produce the best system results at any point in time and over time;
- The aviation mode should be treated in as equitable a manner possible with other modes, from a financial, policy and program approach;
- The varied components of the aviation system should not be assessed or dealt with separately from one another, for public policy purposes;
- In the approach to international air services negotiations, Canada should assure reciprocity of treatment; and,
- In the approach to international air services negotiations, community and regional interests should form the primary public interest criteria.

On the domestic air services front, Manitoba supports greater competition in the industry, balanced by ongoing mechanisms to assure the protection of consumers in the event of market failure or abuse by carriers.

Manitoba favours further liberalization of international air services, including negotiation with the United States on further liberalizing the “Open Skies” treaty. Manitoba, while generally supporting liberalization of international air-cargo services, is however concerned that introduction of cabotage-like liberalization of transborder services holds the potential to put the Canadian air cargo industry at a competitive disadvantage versus the U.S.

The financial viability of the aviation system is a critical issue, the proper treatment of which requires the federal government to reduce or eliminate its excessive extraction of revenues from the system. At the same time, Manitoba encourages the establishment of a redistributive funding mechanism to assure the viability of the nation’s small airports, with reasonable governance and regulatory systems that respect the competitive arena in which airports and the air system operates.

Summary of Recommendations

Domestic Air Services

- *Manitoba recommends that the impacts and effects of reciprocal provision of the “right of establishment” of a domestic service using Canadian employees and equipment, be assessed by the federal government.*
- *Manitoba recommends that the 25% foreign ownership limit for Canadian carriers be raised to 49%.*
- *Manitoba recommends that the federal government, in concert with the airline industry, take steps to implement a national passenger protection program to deal with cases when an airline goes out of business.*

International Air Services

- *Manitoba recommends that the federal government strive, through bilateral agreements or other means, to liberalize the provision of international air services (on a reciprocal basis), especially in regards to the cities, communities and regions allowed to be served by carriers of either country.*
- *Manitoba recommends that the federal government, in concert with other national governments and relevant international institutions, assess and remove current non-transport impediments to increased international air carrier competition.*

Canada-US Air Transport Agreement

- *Manitoba recommends that the federal government enter into negotiations with the United States on further liberalizing the Canada – U.S. Air Transport Agreement (on a reciprocal basis).*

Air Cargo

- *Manitoba recommends that the federal government not pursue direct or indirect cabotage under the Canada – U.S. Air Transport Agreement for the all-cargo air services market.*

Airports and Aviation System

- *Manitoba recommends that airport rents should be eliminated, or be substantially reduced.*
- *Manitoba recommends that any new airport legislation be developed in a transparent manner with consultations with all stakeholders.*
- *Manitoba recommends that the Government of Canada take immediate measures to ensure the long-term viability of small airports in the context of the airport system as a whole.*
- *Manitoba recommends that the Air Travellers Security Charge be eliminated.*

Introduction

Manitoba welcomes the opportunity to provide a submission to SCOT on the issues of air liberalization, airport governance, financial viability and rents, and the viability of smaller airports.

The task you have before you as Parliamentarians is important, as aviation is a vital transportation sector that connects the regions of the nation together, and in turn, our nation to the world. The establishment of a sound domestic and international aviation policy framework is critical, and we are pleased that SCOT will help shape the aviation system for the 21st century.

Manitoba Context

Manitoba is well positioned to comment on what constitutes an appropriate policy framework supporting our aviation transportation system. Our relatively small population necessitates that our industries and businesses must export and connect with external domestic and foreign markets for survival and growth. Winnipeg, as our major commercial centre, is geographically isolated from other major national and continental centers of commerce, thereby necessitating efficient air links to support our business and tourism community.

Winnipeg International Airport (WIA) is the only National Airport System (NAS) airport in Manitoba. It generates about \$300 million in local airport-related expenditures. Winnipeg airport is Canada's only major international airport between Toronto and Calgary and is competitively positioned as a 24-hour unrestricted airport. WIA handles more than 3 million passengers, over 150,000 aircraft movements, and over 140,000 tonnes of cargo annually. Over 7,000 jobs are directly dependent on airport activity, resulting in roughly \$250 million in total labour income on an annual basis. Nearly 21,000 jobs in total are airport-related, for a total payroll of \$780 million per year. Including indirect and induced impacts, Winnipeg International generates \$2.6 billion in economic activity.

As defined in the National Airports Policy, there are 8 Regional/Local airports (Brandon, Dauphin, Flin Flon, Gillam, Lynn Lake, Norway House, The Pas, and Thompson), one small airport (St. Andrews), and one remote airport (Churchill) in Manitoba.

The aviation system in Manitoba is unique in that there are isolated communities in northern Manitoba for which air services are the only year-round transportation service available. In recognition of the importance of aviation to our remote and northern communities, the province contributes by owning and operating 24 small airports at a cost of over \$10 million per year. These small airports are also instrumental in the provision of essential services such as forest fire protection, medevac, and search and rescue operations. Manitoba is also a hub for air services into Nunavut, and for Canada Post's Northern Food Mail program into that Territory.

These factors have heightened—more so than many other jurisdictions—our need for a wide array of effective and efficient transportation options in aviation.

The air mode is also a major employer and contributor to the Manitoba economy. Commercial aviation in Manitoba contributes more than \$580 million annually to the Gross Domestic Product (GDP). Over 9250 person-years of employment are created and maintained by the sector, generating \$370 million of labour income. These figures exclude our aerospace sector and its gross earnings of over \$1 billion annually.

In all, our economy and society are dependent upon the aviation sector, from an economic development, social connectivity, tourism, mobility and business market-access perspective.

Aviation and Economic Development

The air transport sector provides economic development opportunities in its own right for each region of Canada. The framework SCOT recommends should flexibly support regional economic development efforts.

For example, a strategic intent of the Province is to further develop Manitoba as an air cargo transportation gateway for North America—particularly with respect to air cargo—and to capitalize on our advantageous north-central continental location and the I-29, I-35 mid-continent trade corridor that runs from Manitoba through the heartland of the U.S. to Mexico.

In this respect, we supported and are pleased that WIA was recently provided international air cargo transshipment designation by Transport Canada; the only western airport to be so designated to date. Manitoba and its air sector partners also seek to develop an “inland port” at the airport location. The intent here is to develop an integrated facility for air-truck intermodal connections, replete with foreign trade zone designation and a one-stop shop for all transportation, warehousing and value-added activities and logistical needs.

As a adjunct to this effort, Manitoba is pursuing the development of air cargo polar routes, particularly with Russia. For example, Manitoba has signed a letter of intent with the Russian Province of Krasnoyarsk to jointly work toward polar air cargo development. As well, with the support of the Russian Ambassador to Canada (His Excellency Georgiy Mamedov), strong interest has been elicited from Russian airlines to potentially establish polar air cargo flights to and from Winnipeg.

Principles for an Approach to the Aviation Sector

Manitoba recommends that SCOT’s approach to the aviation sector be predicated on several principles, many of which are referenced in the National Policy Statement contained in the Canada Transportation Act.

- **Serve Shippers and Travellers:** The primary objectives of the aviation system should be to serve the needs of travellers and shippers, and to maintain the economic well-being and growth of Canada and its regions. Any SCOT recommendation should be measured against this yardstick.

- **Competition:** Manitoba believes the objectives of serving the needs of shippers and travellers and the well-being of our regions is best achieved where the aviation policy framework provides for as open and fair competition amongst air carriers as reasonably possible. Competition domestically and internationally will produce the best system results at any point in time and over time.
- **Equitable Modal Treatment:** The air mode does not exist in a vacuum, but is also in competition with other modes. In framing its financial and policy recommendations, SCOT should be cognizant to treat the aviation mode in as equitable a manner possible with other modes. This speaks, for example, directly to the issue of federal revenue extraction that is occurring in the aviation mode and the need for federal re-investment support into the aviation system, particularly for small airports.
- **An Aviation System:** All components of the aviation system are interrelated, where an issue or approach in one segment of the system does affect each of the other parts. For policy and program development purposes, the varied parts of the system—ranging from navigational issues to airports to international treaty negotiations—should not be assessed or dealt with in isolation.

Manitoba maintains that any approach to international/transborder aviation must be based on two further key principles, in addition to the principles mentioned above.

- **Reciprocity:** Reciprocity of treatment should be a major tenet of all international air bilateral agreement negotiations, so as to ensure the Canadian air industry is treated in a fair manner, can compete on level playing field with foreign carriers, and can avail itself of expansion opportunities.
- **Community and Regional Interests:** The federal government should adopt a broad public interest criteria to inform its negotiation approaches. This public interest criteria—while clearly recognizing the need to protect Canadian air carrier interests—should give predominance to the needs and objectives of communities and regions. Such an approach is reflective of the principle that aviation should primarily serve the needs of travellers, shippers and the economic objectives of Canada’s regions.

Liberalization

The Minister of Transport referred to SCOT many issues relating to air liberalization. While Manitoba will not deal exhaustively with each of the issues that come under the rubric of “liberalization”, there are several key areas that are very important to the province.

In keeping with our principles set out above, Manitoba generally holds that establishing a framework that permits competition in the air sector is the best means to achieve the best service and rate benefits to shippers and travellers.

The air industry structure is unique in that the treaty negotiation requirement of international air travel imposes limits on international competition between carriers, and also competition

between Canadian carriers on foreign routes. The industry operates as two markets—domestic and transborder/international. We address each to determine how competition in the air sector can be promoted.

Domestic

Domestically, the situation remains rather volatile, and subject to significant shifts in market share, carrier entry and exit, and services and rates—as witnessed by the fall-out of the JetsGo bankruptcy. Compared to a few years ago, when Air Canada held a dominant market share, new and growing entrants in recent years have seized more market-share, creating a relatively more competitive situation and balance in the current air services market.

That being said, means must be sought to encourage even further the objectives of a viable and competitive industry structure. The federal Transport Minister’s referral to SCOT raised the questions of changes in foreign ownership limits of Canadian carriers, rights of establishment and/or cabotage as possible mechanisms to encourage competition. Of the possible measures raised by the Minister, Manitoba asserts that rights of establishment—permitting a foreign investor to establish Canadian domestic services using Canadian employees and equipment—should be investigated as a reasonable next step measure, subject to reciprocating rights with other nations to whom the right may be provided.

Manitoba recommends that the impacts and effects of reciprocal provision of the “right of establishment” of a domestic service using Canadian employees and equipment, be assessed by the federal government.

As well, Manitoba maintains that the current 25% foreign ownership limit in Canadian carriers prohibits greater investment in the Canadian aviation industry and precludes existing carriers’ expansion and renewal, and new entrant growth opportunities.

Manitoba recommends that the 25% foreign ownership limit for Canadian carriers be raised to 49%.

Competition, while generally positive, can create instability and unpredictability in the market-place, resulting in ever-changing city-pairs, rates, frequencies, aircraft gauge, and even carriers themselves. For example, while consumers benefited from JetsGo’s existence as a discount carrier through lower fares, its bankruptcy caused much hardship to many Manitobans and Canadians, who had booked and pre-paid for flights beyond the date JetsGo ceased operations. As a protection to travellers and shippers in a new competitive era in the domestic air services market, the federal government should consider the creation with the airline industry of a framework to recompense travellers in the event of carriers ceasing operations.

Manitoba recommends that the federal government, in concert with the airline industry, take steps to implement a national passenger protection program to deal with cases when an airline goes out of business.

Lastly, Manitoba asserts that the federal government should continue to ensure the Canadian Transportation Agency and Competition Bureau have the appropriate tools and resources to deal with any market abuses by carriers.

International

The international market is circumscribed by the 1944 Chicago Convention requirement that only national governments, on a bilateral basis, can negotiate carriage rights and designate the specific carriers to fulfill those rights. In other words, it is far from a free and competitive market, even though an adequate number of large international carriers exist to allow for competition in the marketplace.

One of the underlying premises of the National Airports Policy (NAP) devolution initiative was that local communities, via their airports, would be able to market themselves and their regions to attract services and undertake economic development opportunities. Certainly, Manitoba and our Winnipeg Airports Authority have attempted to do so by developing as a North American air cargo hub, and the airport has successfully marketed to airlines additional and new passenger services where bilaterals permit (e.g, recently introduced Zoom Airlines Winnipeg-London, UK service).

Nonetheless, the combination of Canada's international air transportation policy and the global regime of bilateral air transport agreements still proverbially ties one hand of the airport authorities and communities behind their backs. For example, most bilaterals exclude most Canadian airport cities, effectively precluding airport authorities and the communities from even being able to market their destinations in most foreign countries. Winnipeg was notably the first Canadian airport to receive its designation as an international airport in 1928, yet it is not listed as a point of service in many of Canada's bilateral agreements. Manitoba also has a concern that in its bilateral negotiations, the federal government does not permit community or regional representatives an effective avenue for participation (unlike the air carriers). This situation should be addressed.

Ideally, in an open global market, any carrier of any nationality would be allowed to fly between any two airports in the world, subject only to the rules implemented for traffic control and safety. However, we recognize this is not likely to happen soon. The focus then is for government to liberalize all restrictive bilaterals as soon as possible.

In the absence of global open skies or multi-national open skies agreements, Manitoba advocates that the federal government continue to strive to achieve bilateral air service agreements which are as unrestricted as practicable. Manitoba urges that Canada should continue to negotiate bilateral air transportation services agreements, to permit for increased numbers of international flights by carriers of either nationality between Canada and other countries. The "Open Skies" agreement between Canada and the United States, for example, is a revolutionary and progressive treaty. Transborder travel has increased and additional services are being provided to meet the demand. This regime has benefited carriers, travellers, shippers, consumers and producers. Clearly, more "open skies" are needed.

In its negotiations, Canada must consider that if no Canadian air carrier is interested in serving an international route, a foreign carrier should be allowed to operate the route without the requirement of a specific benefit to a Canadian carrier. We would like to see more international agreements that permit service from any point in one country to any point in the other country, as in the Canada-U.S. agreement. This would allow more Manitoba communities with airports to market their destinations in a unique fashion. For example, polar bears, whale watching and the aurora borealis are attractions drawing people from around the world to Churchill, Manitoba—the tourism potential of which could be further enhanced by direct scheduled flights from foreign origins to Churchill.

Some parties might point to Canadian carrier viability concerns in the face of any such actions. We are cognizant of these concerns, but believe Canadian air carriers are capable of competing on a global scale provided a level playing field is established and maintained. Air Canada is one of the top 20 largest air carriers in the world, and has a world-class reputation as witnessed by a number of international awards. Air Canada would agree that it, in particular, has been able to reap substantial rewards when skies are “opened”, as witnessed by its U.S. transborder success. The number of Canadian charter and discount carriers that have recently entered and expanded in the domestic market should further be allowed to take advantage of international opportunities.

Manitoba recommends that the federal government strive, through bilateral agreements or other means, to liberalize the provision of international air services (on a reciprocal basis), especially in regards to the cities, communities and regions allowed to be served by carriers of either country.

Through the International Air Transportation Association and the International Civil Aviation Organization and other organizations, Canada must work to eliminate other undue interference in the market, such as the regimentation of schedules and frequencies, aircraft gauge, fares, city pairs, and other international practices that restrict competition and inhibit carriers’ abilities to rationalize services and prices with demand. Regulations pertaining to security, citizenship, nationality, customs and immigration can be valid, but again, all need to be examined for unintended consequences to the supply of efficient and competitive international air transportation services.

Manitoba recommends that the federal government, in concert with other national governments and relevant international institutions, assess and remove current non-transport impediments to increased international air carrier competition.

Transborder

Manitoba welcomed the February 24th announcement by Transport Canada Minister Lapierre and U.S. Transportation Secretary Mineta to begin exploratory talks on further liberalization of the Canada–U.S. Air Transport Agreement, and the subsequent May 26th announcement by Transport Minister Lapierre to hold a consultative round of discussions with stakeholders on the treaty.

The “Open Skies” agreement of 1995 between Canada and the United States has proven to be beneficial to shippers/receivers, business and leisure travellers, tourism operators, consumers, airports, communities, and air carriers on both sides of the border. We see no reason why expanding the agreement should not enhance these benefits, subject to the principles Manitoba has espoused throughout the submission.

Manitoba recommends that the federal government enter into negotiations with the United States on further liberalizing the Canada – U.S. Air Transport Agreement (on a reciprocal basis).

Air Cargo

In consideration of the differing characteristics between the air freight and passenger sectors, Manitoba believes the all-cargo air services sector should be treated uniquely. Given Manitoba’s interest in the development of Winnipeg as an air cargo hub, Manitoba generally favours the greater liberalization of international bilaterals governing air cargo, again on a reciprocal basis, and again with a federal negotiation focus on flexibility in city points to be served.

With respect to transborder services, however, there remains a concern that any form of cabotage may disadvantage the Canadian industry and especially communities, such as Winnipeg, that are hub operations for our east-west cargo networks. Why so? The institutional and structural framework in which the U.S. industry operates may effectively preclude a fair and level playing field for Canadian companies, airport authorities and communities in a continental market. For example, the dominant players like UPS and FedEx have extensive economies of scale via their U.S.-based hub operations and supporting non-air infrastructure that likely cannot be matched by Canadian players. As such, Manitoba does not support at this stage the consideration of any type of cabotage—full, modified or indirect—in the Canada-U.S. air cargo services market.

Manitoba recommends that the federal government not pursue direct or indirect cabotage under the Canada – U.S. Air Transport Agreement in the all-cargo air services market.

Airports and the Aviation System

Manitoba believes much of the efforts in the last two decades—deregulation of the domestic air services market, airport and air navigation system devolution, the Open Skies Treaty—have been reasonably sound public policy in concept.

However, any policy framework, especially one that creates a more deregulated regime, must be accompanied by a supportive fiscal framework for the system as well. In this respect, Manitoba is concerned that the federal government practice of extracting revenue from the aviation system (more than its investment in the system would reasonably warrant) is rendering many of these positive federal initiatives as moot. This is resulting in a financial deficit that is undermining the competitiveness and viability of our aviation transportation system.

This practice and approach should be addressed because it violates several aspects of current national transportation policy established in the *Canada Transportation Act*. Firstly, the federal extraction of revenue from the aviation system limits the ability of the air sector to compete with other modes. It contravenes the condition that each carrier or mode should receive fair and reasonable compensation for the resources it is required to provide as a public duty. Thirdly, it breaches the need to have policies in place that permit economic viability for the mode. The solution is to ensure monies extracted from the air mode are reasonably rededicated to the mode, or that such extraction is dramatically lessened.

Airports

Manitoba agrees that the federal devolution of airports to locally managed entities can and has better served the public interest. However, the withdrawal of federal control of airports has not been accompanied by a concerted effort to establish a policy and fiscal framework that permits these local airport entities to flourish.

NAS Airports

Indeed, a premise of the National Airports Policy was that the Government of Canada would be “financially no worse off”. Before NAP, airport ownership, operation, and maintenance was costing Transport Canada about \$200 million annually. The airports are now paying more than \$250 million in rent each year. The Government of Canada is more than \$450 million better off on an annual basis. Despite the welcome rent relief announcement of May 9th by the federal Minister of Transport, the fact is revenue to the federal government from rents will still increase over time, as more airports pay rent and rates increase. More still needs to be done.

This rent revenue practice has forced airports to implement and increase passenger fees, and landing and terminal charges to maintain viability and provide for capital programs, at an overall cost to the aviation system. The federal government, as the landlord, brings nothing to the arrangement except land ownership. In most cases these federal lands were encumbered by outdated facilities at, or nearing the end of their useful lives. Airport authorities have invested almost \$9 billion in capital improvements to airport infrastructure since transfer.

Manitoba sees no reasonable rationale to justify the continued collection of rent by the federal government from National Airport System (NAS) airport authorities.

Manitoba recommends that airport rents should be eliminated, or be substantially reduced.

Small Airports and Viability

Two recent studies into the viability of smaller airports—one commissioned by the Provincial Transportation Departments and one by Transport Canada—arrived at essentially the same conclusion. About half of the airports studied are unable to meet their operational requirements,

let alone make a contribution to capital, indicating that some form of external funding for small airports is required.

The federal government is deriving more than sufficient revenues from the airport and air transportation system to ensure the maintenance of the overall system of airports. Through an enriched Airport Capital Assistance Program or via other redistributive mechanisms, the federal government should return some funds into the small airport system to reasonably support its viability.

Manitoba remains concerned that the small airports system should not be offloaded by the federal Ministry of Transport into other sectoral or regional programs, and that they continue to be supported by Transport Canada as an essential part of the overall aviation system in Canada.

Manitoba recommends that the Government of Canada take immediate measures to ensure the long-term viability of small airports in the context of the airport system as a whole.

Airport Governance and Regulatory Framework

The issue of airport governance and the safety and security regulatory framework under which they must operate also has an impact on the viability of the overall aviation system.

The proposed *Canada Airports Act* (Bill C-27) which died on the Order Paper when Parliament prorogued in December 2003 was criticized by airport authorities as prescriptive and onerous. Manitoba believes a more transparent and participatory consultation process by Transport Canada in advance of the development of proposed airport governance legislation will result in a better framework for the future.

Manitoba recommends that any new airport legislation be developed in a transparent manner with consultations with all stakeholders.

Airports are subject to numerous safety and security regulations. To assure that such regulatory developments are cognizant of the competitive environment in which airports operate, caution and balance must be exercised by the federal government to assure such regulations—witness the numerous industry concerns expressed with respect to the Canadian Aviation Regulation 308—are not overly onerous. Manitoba maintains a need for Transport Canada to establish an adequate consultation and benefit-cost analysis process for any such efforts. Overall, Transport Canada should work with stakeholders to develop more acceptable regulations that reasonably balance safety requirements with the costs imposed on airports and air carriers to meet such regulations.

Lastly, the impacts of the federal government policy of requiring airports to provide space and services to federal agencies such as Canadian Air Transport Security Authority and Canadian Border Services Agency (CBSA) free of charge tends to reduce airport viability by increasing costs. An impediment to attracting new transborder or international air services exists in the full cost recovery policy of CBSA, which Manitoba notes creates an inequity between those airports that already have CBSA services, and those that currently do not.

Air Travellers Security Charge (ATSC)

While safety and security are paramount and not to be compromised, Manitoba is concerned about who pays for transportation security enhancements since the events of September 11, 2001.

We assert that payment of the Air Travellers Security Charge by air passengers is unreasonable, despite having been reduced in recent budgets. Travellers pay the ATSC, although beneficiaries include people on the ground and in buildings.

Users of other modes of transportation are not being charged specific fees for enhanced security. Revenue from the fee is not dedicated to air transportation security nor collected by the Canadian Air Transport Security Authority (CATSA), but accrues to the federal government general revenue account. The fee level and the revenue generated are apparently not related to the costs of the enhanced security measures. For example, ATSC revenue for the year ended March 31, 2003 exceeded by \$234 million the amount required, according to Federal Department of Finance.

Payment of federally imposed security costs by users of smaller airports or residents of communities they serve tends to reduce the viability of such airports. Fair competition between modes is distorted as users of other modes are not subjected to a separate fee, although security has been enhanced in other modes and at land border crossings.

While enhanced security measures help boost consumer and public confidence in air travel, the ATSC acts as a deterrent to air travel and impedes the recovery of the air transportation industry from the effects of such events as 9/11, SARS, and the US-Iraq matter. The flat fee is also disproportionate on shorter flights with lower fares.

Manitoba recommends that the Air Travellers Security Charge be eliminated.

Conclusion

Manitoba appreciates SCOT having undertaken this exercise to assess air liberalization, the airport sector and the health of the system overall. Manitoba asserts that the approach outlined in our submission will result in a better framework for the aviation industry domestically and internationally, to the ultimate benefit of Canadian travellers, shippers, regions and communities.