

# IN BRIEF



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## Air Transport Policy in Canada: Potential Directions?

### INTRODUCTION

In January 2004, air transport industry stakeholders attended “Air Currents: Building the Future for Canada’s Air Transport Policy,” a conference that took place in Ottawa. More than 100 industry, public sector and academic delegates participated to discuss future policy directions for Canada.

In his speech at the conference opening, then Transport Minister Tony Valeri challenged the audience to present ideas on policy options for international air transport that focussed on market forces, consumer needs and Canada’s relationship with Europe and the United States. The delegates responded by making recommendations concerning what they collectively determined are the five most important air transport policy objectives facing the Canadian government today:

1. Airport fees and charges;
2. Security and pre-clearance measures;
3. “Open skies” agreement with the United States;
4. Rules with respect to foreign ownership of Canadian airlines; and
5. Canada’s participation in a Transatlantic Common Aviation Area.

Some background on each of these policy areas and the key recommendations that resulted from the conference sessions are provided in the sections below.

### AIRPORT FEES AND CHARGES

Conference participants cited airport rent and the air travellers security charge (ATSC) as the most controversial fees and charges at Canadian airports.

### A. Airport Rent

The federal government charges, or will soon begin charging, rent to the operators of all National Airports System (NAS) airports. These 26 airports, leased from the federal government by not-for-profit, non-share capital airport authorities, handle more than 90% of Canada’s total air traffic. The federal government collected nearly \$225 million in airport rent in 2003, and the amount is scheduled to increase to nearly \$350 million by 2007.

The airport industry thinks that the government collection of rent on airport assets is not justifiable. One reason is that Transport Canada used to operate the airport system at a loss, so rent is not replacing an income stream. Another is that the cumulative rent paid to date allegedly exceeds the value of the assets that were transferred. Furthermore, to the extent that economic growth depends on low-cost transportation, further growth in airport rent payable could have a negative impact on the future of the Canadian economy. Airport rent raises the costs of air travel and freight services which are critical to economic activity.

The President of the Canadian Chamber of Commerce proposed a number of measures with respect to airport rents that were in line with the recommendations of the House of Commons Standing Committee on Transport in April 2003:

- (1) The government should suspend rental payments by the airports for a two-year period and the airports should pass the rental savings on to the air carriers;
- (2) A more transparent process for determining airport rents should be established;

- (3) Rents should be based on the real cost and expenses incurred by airport operators – leading to a substantial decrease in rents;
- (4) There should be a cap on the total rent that the Government of Canada extracts from individual airports; and
- (5) All airport rents should be directed into an “airport reserve” rather than into the Consolidated Revenue Fund.

## **B. The Air Travellers Security Charge**

The Canadian government collected over \$420 million in 2002-2003 from the ATSC. Although the charge has been reduced twice since it was implemented in April 2002, it still exceeds that of the United States. The ATSC is currently \$7 for a one-way domestic flight, \$10 for a transborder flight and \$20 for any other international flight. By comparison, the charge in the United States is US\$2.50 per flight segment, to a maximum of US\$5.

Conference participants reiterated what the industry has typically argued: that air transport security benefits the general public and should be paid for out of the public treasury. They further recommended that the government revisit the unanimous recommendations made by the House of Commons Standing Committee on Transport in April 2003. Those recommendations identify other opportunities to make progress toward relieving the burden of charges, excise taxes and rents faced by the air transport industry.

## **SECURITY AND PRE-CLEARANCE MEASURES**

Airlines have a commercial imperative to ensure that passengers experience convenient and swift processing at the airport. In the new aviation security environment, passenger processing has become an operational challenge. Although the task of passenger screening at airports, previously the responsibility of the airlines, was reassigned to the Canadian Air Transport Security Authority in December 2001, airlines have been given new responsibilities. Airlines are now compelled to ask passengers to verify the contents of their baggage at check-in and to present photo identification prior to boarding the aircraft. Enhanced passenger screening and airline procedures have increased inconvenience for passengers and the demands on their time.

Conference participants, while concerned about the impact of security measures on passenger processing, did not recommend any changes to the current policy at airports. (For example, Canada’s Smart Border Declaration of December 2001 details government intentions to establish a secure system that will allow low-risk frequent travellers between Canada and the United States to move efficiently across the border.) They were, however, concerned about the impact of the costs of security measures on demand for air services.

## **“OPEN SKIES” AGREEMENT WITH THE UNITED STATES**

It has been almost 10 years since Canada and the United States signed the “open skies” bilateral air agreement. Although it is more restrictive than the open skies agreements between the United States and other countries, the Canada-U.S. agreement has enabled growth in Canada-U.S. traffic from 13 million passengers in 1994 to over 20 million passengers in 2001.

Conference participants felt that it is time for Canada to renegotiate its open skies agreement with the United States and pursue an “Open Skies Plus” regime. Open Skies Plus, a concept developed by Air Canada, would build on existing transborder operations in two important ways. Firstly, carriers from Canada or the United States would be allowed to market domestic routes in the other country by routing them over a hub in the airline’s country of origin. Secondly, it would also allow dedicated cargo flights to serve two or more consecutive points in the other country. Currently these practices are prohibited in the bilateral agreement.

## **FOREIGN OWNERSHIP RULES**

Popular opinion on foreign ownership rules has been divided in Canada, due to the state of the domestic airline industry in recent years. Air Canada’s uncertain financial position has led policy makers to be especially cautious in making significant regulatory changes. However, others feel that bold reform to ownership rules is necessary at this time to provide Canadian carriers with broader access to foreign investment capital. Advocates of higher foreign ownership limits believe that raising the current limit of 25% will result in greater choice in services, to the benefit of Canadian consumers.

Conference participants supported raising foreign ownership limits to 49% for international operations and eliminating them for domestic operations. In order to make this possible for international operations, Canada would have to substitute a “principal place of business” clause for the current “substantial ownership and effective control” clauses defining carriers’ eligibility to benefit from the rights under bilateral air service agreements.

## **CANADA’S ROLE IN A TRANSATLANTIC COMMON AVIATION AREA**

The Association of European Airlines first introduced the concept of the Transatlantic Common Aviation Area (TCAA), a new and very liberal regulatory framework between the European Union (EU) and the United States, in 1995. The concept was slow to develop until it recently became necessary to renegotiate a number of bilateral air service agreements between EU member states and the United States. The catalyst was a ruling by the European Court of Justice in November 2002, which found that the nationality clauses enshrined in the bilateral agreements were in violation of the Treaty Establishing the European Community.

Conference participants felt that the existence of a TCAA that excluded Canada would be detrimental to Canadian carriers. They recommended, therefore, that Canada should look for opportunities to participate or signal approval or dissent during the process, even though the talks are limited to the United States and the European Union at this time. If participation in the talks is not possible, they recommended that Canada initiate its own discussions with the European Union.

## **CONCLUSIONS**

Three of the conference participants’ key recommendations incorporated the concepts of market forces, consumer needs and Canada’s relationship with Europe and the United States, as per Minister Valeri’s challenge. These were:

- Canada should renegotiate with the United States to achieve “Open Skies Plus,” a more liberal bilateral air service agreement than currently exists.
- Foreign ownership limits should be eliminated for domestic operations and raised to 49% for international operations.

- Canada should monitor the Transatlantic Common Aviation Area talks between the EU and the United States for the purposes of a) planning its own negotiations with the EU, or b) participating.

The recommendations with respect to the other two important policy areas identified by the conference participants had to do with government involvement in the industry. These were:

- Government-induced costs facing the air transport industry (i.e., airport rent, user charges, excise taxes) should be reduced.
- Security measures and customs pre-clearance must be streamlined.

Some of these questions are already on the government’s radar. In July 2003, the Government of Canada provided short-term relief to airports by deferring some or all of the money owed for rent or airport assets for a couple of years, interest-free. Also, the Government of Canada reduced the ATSC for the second time in the 2004 Budget. Furthermore, Transport Canada has promised to deliver a review of the airport rent policy this year.

## **REFERENCES**

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