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Air Industry Priorities: Renewed Focus on Passengers and Growth

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1. Introduction

- a. As you may know, I was the Deputy Minister of Transport Canada during the mid-1990's.
 - i. The government of the day was under significant financial pressure.
 - ii. Among other measures, it undertook an aggressive commercialization strategy that resulted in major structural changes in the air sector.
 - iii. What has not happened since then is a policy mechanism to trigger a full review of these commercialization and cost saving initiatives on the industry over the past 10-15 years.
 - iv. What has transpired is a systematic shift of the government towards viewing the industry as a source of revenue as opposed to an economic driver.
 - v. I applaud the efforts of this Committee in undertaking this review. It is far overdue and a necessary step in putting the appropriate balance back in the system.
- b. As you know, this industry has done reasonably well over the past few decades, despite many ups and downs
 - i. Increases in passengers and cargo in all air sectors.
 - ii. Deregulation; more competition and new entrants; several open skies agreements.
 - iii. Relatively low air fares and slow increases compared to the Consumer Price Index.
 - iv. Privatization of airlines and commercialization of airports and air navigation.
 - v. Expansion of the major airports and private investments in airport activities.
 - vi. Enhanced safety and security.

- c. However, as the Committee has heard from other witnesses, the industry can perform much better. It is being held back by four main burdens and inhibitors to growth.

2. Financial Burden on airlines and airports and ultimately on passengers and cargo.

- a. In fiscal 2011, the federal government will likely collect from the air sector an estimated \$1 billion in special charges, over and above normal business taxes, mainly from airport rent, air security charges, and fuel excise taxes.
- b. Plus the costs airlines, passengers and cargo, through higher fares, pay for air navigation services (\$1.1 billion).
- c. Most airports also charge airport improvement fees on each ticket, costing anywhere from \$5 to \$25 per passenger, the highest being Toronto's Pearson Airport.
- d. Passengers pay not only the air fare and the airport improvement fees BUT also:
 - i. A security charge from \$7 to \$ 16 per passenger based on routes and distance;
 - ii. A fuel surcharge;
 - iii. NAV Canada surcharge from \$ 7 to \$20 based on distance;
 - iv. An Insurance Surcharge of \$ 3; plus of course
 - v. Charges for advance seat selection, extra or overweight baggage, meals, pillows, blankets and other items, most of which were free not that long ago.
- e. Passengers also cover the costs, one way or another, of rather inflated salaries and benefits for Canadian airport CEOs, Board Chairs and Members; several airport CEOs receive from \$ 250,000-700,000 annually, chairs as much as \$ 150,000 and some board members \$ 60,000 per year for supposedly community and service based entities.
- f. As the Committee has heard, over the past 10 years the federal government has extracted over \$7.0 billion out of the air transport industry. During the same time, the government has poured almost \$2.6 billion into VIA Rail Canada, a network that carries only 15% of the domestic passengers carried by airlines in Canada.
- g. Air passengers are getting "loonied" and "toonied" for every flight: many are unhappy, traveling less, going to the US or staying home.

- h. These high costs are also obstacles to Canada's major airports becoming real international hubs and transit points. Passengers can afford base ticket prices and airlines most of the landing fees but neither can afford all of the extra fees and taxes they are forced to pay.

3. Restrictive International Air Agreements.

- a. International air agreements are the last vestige of 18th Century Mercantilism: all is forbidden unless expressly agreed to between countries: landing rights, routes, frequency, types of services, number of passengers, etc.
- b. Announcements about minor air bilateral agreements are a dime per dozen and a cottage industry for air negotiators within and outside government.
- c. Many types of air freedoms exist but all are anti-competitive, out of date and restraints on air growth. A few examples:
 - i. When Air Canada decided to stop its service to Singapore, Singapore Airlines had to stop its service to Canada too;
 - ii. Despite the claim of Open Skies with the USA, Air Canada is not permitted to board passengers in Los Angeles on a route from Toronto to South America or Asia.
 - iii. Again despite the new so-called Open Skies agreement, Canadian airlines cannot fly passengers between cities in the US or within Europe and vice versa.

4. Foreign ownership restrictions

- a. Canada only allows 25 % foreign ownership in our airlines. The Governor-in-Council may, under special circumstances, increase this to 49 % but this authority has not been implemented yet. We do not do that in retail, manufacturing, oil, gas, automobiles, etc. What is so special about airlines?
- b. It discourages competition, restricts access to foreign capital and blocks more integrated air alliances and airline mergers. It is happening in Europe; why not in Canada and North America?

5. Air Security System

- a. Canada has an extensive and expensive air security system
 - i. CATSA has become a large organization (Responsible for security screening at the 89 designated airports in Canada; 538 employees, outsources screening services to private security companies, more than 6,000 screening officers who screen about 48 million passengers and 62 million pieces of luggage).
 - ii. In Canada, airline passengers have to cover all security costs, unlike most other jurisdictions. The idea that travelers and shippers should pay “user fees” to have themselves protected from terrorism seems inappropriate. It is the State that is the target of terrorists; the air sector only the means. We don’t charge a special security fee to protect our citizens from terrorists when they enter a large building, ride a subway or when they visit a sports facility or a museum.
 - iii. Even with many increased security protocols, all is definitely not well. The Senate Committee on Security and Defence, various industry audits and the media have pointed out the inadequacy of airport staff security clearance, the lack of trained airport employees who are supposed to be identifying suspicious persons or potentially dangerous contents in carry-on items and the ease with which perimeter security at airports can be breached.
 - iv. The current system focuses too much on luggage and not enough on actual passengers and those that are more likely to be problematic. As an Israeli airport security expert stated not long ago: “People are the dangerous part of the business, not their luggage. People who come to inflict harm act differently than a benign traveller.”
 - v. The recent review of CATSA has recognized this and has recommended major changes. Some recommendations include that CATSA needs to develop a policy on screening all cargo, should move towards Passenger Behaviour Observation, and implement new procedures and more courses to screening officers on smarter and faster processing and new screening techniques.

6. New Policy Directions

- a. Given the above, it is clear that new policies are needed. Despite budget deficits and obstacles and opposition to some of the required action, I suggest the government, airports and airlines should focus on the following over the next 3-5 years.
- b. Reduce over three years the financial burden for the industry and for passengers:
 - i. Phase out all airport rents;
 - ii. Eliminate the excise fuel tax, federally and provincially;
 - iii. Fund at least half of the costs of air security from government; and
 - iv. Ensure that reduced charges for airports and airlines are passed on to passengers through a 2 for 1 deal:
 1. For every dollar the government reduces rents, fees and taxes for the air sector, passengers should get 50 cents of the benefit.
 2. If airport rents are eliminated, the airport improvements fees to passengers should then be reduced by 50 %.
 3. Ditto for the elimination of the jet fuel excise taxes charged by the federal government and subsequently by provincial governments. Half of the benefits should go to reduced fuel surcharges on airline tickets.
- c. Negotiate true Open Skies agreements with other like-minded jurisdictions
 - i. Allow all airlines to fly wherever and whenever they want for passengers and cargo – domestic and international;
 - ii. Support increased co-operation and integration among airlines.
- d. Change or eliminate Foreign Ownership Rules
 - i. Encourage more foreign access to capital and investments
 - ii. Allow more partnerships, mergers and take-overs
- e. Air Security
 - i. Reduce the security charge for passengers;
 - ii. Change the focus of air system security to assessing passengers not luggage through more Passenger Behaviour Observation techniques; and
 - iii. Facilitate smarter and faster processing for regular travelers, smaller airports, and for “low” profile passengers.

7. Concluding Comments

- a. The airline industry needs help in attracting more traffic and passengers, and the best way to do this is through the reduction of the financial burden.
- b. A 2 for 1 deal would be beneficial to all stakeholders within the industry;
 - i. Good for airports – reduces or eliminates airport fees so that the money saved can be passed on to passengers, paying down debt, and funding for infrastructure updates. Reduced fees may also attract more transit traffic from international airlines using such airports as Toronto and Vancouver as major international hubs.
 - ii. Savings for the passengers will also mean more people will be able to fly and more revenue will be brought into the airports;
 - iii. Good for the airlines: with a reduction in airport fees, security surcharge and fuel taxes, more travelers will fly;
 - iv. The entire airline industry: with more passengers traveling, the air sector will grow. This should create more jobs within the sector, and produce more revenue for all of the stakeholders.
 - v. The Government of Canada – a reduction in rent, fees and taxes will see many more people travel by air, domestically and internationally. Increased travel and tourism will boost the Canadian economy, and the government will, in time, make more revenue rather than lose it.
- c. Changing air ownership rules and more effective Open Skies agreements will also have positive effects: more competition and choice, more integration and partnerships, and another opportunity for Canada to have major international gateways.
- d. The effects of the changes will not come immediately. Some will take time to implement. However, the long term positives will greatly outweigh the short term financial negatives on government.