



Airline Restructuring in Canada Final Report



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Table of Contents

INTRODUCTION.....	3
HOW IS THE CANADIAN AIRLINE INDUSTRY SHAPING UP?	5
WHAT SHOULD GOVERNMENT BE DOING ABOUT THE AIRLINE INDUSTRY FOR THE LONG-TERM?	8
Air Policy.....	8
National Transportation Policy -- Integrating the modes	28
Other Government Policy that Affects Transportation	29
WHAT SHOULD GOVERNMENT BE DOING ABOUT THE AIRLINE INDUSTRY IN THE SHORT-TERM?	39
Bill C-26	39
Air Canada and the Official Languages Act (OLA).....	53
Fair Treatment of Employees	54
ISSUES AND RECOMMENDATIONS FOR STAKEHOLDERS	56
Collective Action	56
Airlines	58
Airports	61
Urban, rural and remote communities	63
Travel Agents.....	64
Consumers.....	66
SUMMARY OF RECOMMENDATIONS	67
Long Term Recommendations.....	67
Short Term Recommendations	70
Stakeholder Recommendations.....	72
<i>APPENDIX I: DOMESTIC, INTERNATIONAL AND TRANSBORDER MARKETS.....</i>	<i>75</i>
The Domestic Market	75
The International Market.....	79
The Transborder Market	80
<i>APPENDIX II: MEETINGS HELD/INPUT RECEIVED</i>	<i>81</i>
<i>APPENDIX III: MANDATE OF THE INDEPENDENT OBSERVER</i>	<i>83</i>
<i>AFTERWORD AND ACKNOWLEDGEMENTS</i>	<i>84</i>

Introduction

Two years ago, airline restructuring looked relatively straightforward. Once Air Canada acquired Canadian Airlines Corporation, could Air Canada successfully merge Canadian Airlines into its operations? What did that mean for people affected by the airline sector: communities, agents, businesses, and airline employees? A rosy economy led to the hope that after some upheaval, Canada would have an equally rosy airline industry: Air Canada as our strong, international carrier, moving Canadians around the world and into the heart of our communities. Niche carriers providing lower fare options for vacationers and people visiting friends and relatives. Then it changed.

Amid the aftershocks of the events of 2001 – the murderous September 11th attacks, the high-tech meltdown, plunging stock values – we remain unsettled and unsure of exactly where we go from here, and what the world will look like once we arrive.

The airline sector, rather than continuing its expected glorious growth of the mid and late 1990s, was one of the hardest-hit. Travel plummeted. High-yield customers melted away, leaving full-service airlines' pricing and scheduling strategies, keyed to the coveted "front of the plane" traveller, in shambles, along with their revenue projections.

Air travel security, previously a necessary evil positioned between the passenger and the aircraft has become a first line of defence against real evil. The cost of protecting our country from the use of civil aircraft as weapons of mass destruction has fallen on passengers.

Air Canada has had to reinvent itself. Old strategies have been abandoned in favour of a new business template: new brands, new subsidiaries and an attempt to appeal to the previously undervalued low-fare traveller. This radical approach seems to be working.

WestJet rode high on turmoil and change. Growing numbers of consumers chose its low-fare service that got them to their destination pleasantly and with a minimum of fuss. WestJet showed a profit throughout the most difficult of times, including \$12 million for its most recent quarter and was named 2nd top performing "median" airline (i.e. with revenues less than \$4 billion) in the world by the trade publication, *Aviation Week & Space Technology*.

Air Canada has dropped some capacity between 2000 and 2002, which has been picked up by other carriers, especially low-fare jet airlines. As a result, there is more competition on domestic long-haul routes, and more low-fare options. However, it also appears that capacity on short or medium-haul routes has not been replaced, but has been redeployed on longer-haul routes (based on a three per cent decline in "seats" flown, but a five per cent increase in "seat-kilometres" flown).

Airlines started up and failed (Roots Air), expanded too quickly and failed (Canada 3000) and started up (Jetsgo, CanJet). Air Canada announced a \$30 million profit in its second quarter (the only full-service carrier in North America to show a profit) but the company still carries a debt and liability burden of about \$10 billion. While parts of our current economy are stunning, others are just stunned, shattered by the flight from stocks, the high-tech washout and corporate malfeasance, and misfeasance. The U.S. economy and its carriers are not anywhere near a recovery. Not only is there no light at the end of the tunnel yet, we don't know how long it is, how winding or how deep.

We do not yet know what our airline industry **could** be in the future. There are too many uncertainties. However, this does not prevent us from determining what the airline industry **should** be, and what we must do to get there.

There are two ways to examine the airline sector. One is to look at the immediate, short-term changes: how much competition there is; on which routes; the state of carriers' financials, and so forth. The second is to look at the fundamental, framing policy that sets the "rules of the game". The latter impacts not only today's airlines, but tomorrow's as well.

This report, the final of four, recommends actions for both the short and long term. Short term, I have considered the Air Canada acquisition of Canadian Airlines Corporation, and its direct impact on stakeholder groups. The government framework that I have used to create short-term recommendations is Bill C-26, the Air Canada undertakings and other provisions such as the Official Languages Act.

For the longer term, I have examined some of the key policies that affect the airline industry in elemental ways that go beyond immediate concerns and exigencies. Recommendations for long-term action use the government's own objectives as their starting point, which are:

*...for Canada to have an efficient and viable airline industry with **strong domestic and international competitors** and which is **affordable, responsive** to users and their communities and overall, **satisfies the needs of all Canadians**"¹*

The recommendations suggest new approaches for governments, airlines and stakeholder groups, and provide views on what each can contribute to ensure a resilient and competitive airline industry that serves Canadians over the short and long term. The recommendations also deal with the issues of Canadian ownership of carriers, the role of air access in economic development, particularly in remote or rural communities, and the participation of federal government departments and other levels of government to achieve solutions.

¹ 2002-2003 Estimates – A Report on Plans and Priorities, Transport Canada

How is the Canadian Airline Industry Shaping Up?

The acquisition by Air Canada (AC) of Canadian Airlines Corporation (CAC) and the subsequent integration of their operations has been a costly, messy process, made worse by difficulties in merging union groups, post-September 11th jitters, additional security charges and delays and the disappearance of high-yield business demand. Restructuring is not over. It has barely begun.

There are several interesting trends. The first is that despite the different world we live in today, compared with 1999, there has been little change in the overall capacity of the domestic sector². If it were tracking the economy, it should have grown substantially more than it has, even when one considers the impact of 2001.

A second trend is the explosive growth of low-fare options, which has increased from 16% to 36% of seat-kilometres flown between 1999 and 2002. The airline industry is proving surprisingly resilient – the domestic capacity lost with the demise of Canada 3000 has been replaced in less than a year both by existing carriers and by new entrants. This is quite remarkable given today's uncertainties.

The most significant story is that despite everything we have been through, how little the “big” picture has changed. If our goal is the growth of competition, we're not there yet. Perhaps not enough time has passed since the acquisition by Air Canada of Canadian Airlines Corporation. Perhaps 2001 derailed us. Or perhaps, we have reached a state of equilibrium: one dominant carrier with the lion's share, and a number of niche carriers flying along side.

Overall, Air Canada is virtually as dominant today as it was in 2000. Its size is not much different than the combined size of Air Canada and CAC circa 1999 in both the international and transborder markets. There has been little if any competitive growth there – in fact, there have been reductions in the number of Canadian carriers flying either transborder or international.

Domestically, there has been an eight per cent decline in Air Canada's market share attributable to its reduction of capacity when it merged with Canadian Airlines in 2000. Further, there are indications that most of the capacity that was removed was on short-haul routes. Since 1999, total available domestic seats declined by three per cent, but seat-kilometres increased by five per cent.

WestJet has made enormous strides over the last few years, increasing to a 14.16% share from 4.26% of the market between 2002 and 1999. Low fare service, including Tango, is booming – 36% in summer 2002 from 16% in 2000. There was also a

² See charts, Domestic Operating Statistics, Market Share by Seat-kilometre and Seat, pg. 76

significant increase in cities receiving competitive service, increasing from 17 points with year-round service to 24 with year round competitive service in 2002.

Service to smaller communities remains problematical, as the numbers tend to support the contention that service has been reduced to some regions. There may be further reductions when Air Canada is able to vacate communities at the end of this year. While the current capacity may be the "right size" for existing demand from a carrier perspective, there are still issues that are yet to be addressed in regional service to Canadians.

When one looks at airports served by "major jet operators" in the south of Canada, over half are served by more than one carrier: 39 compared with 35 served by one airline only. When one includes airports served by turboprop aircraft, including those in the north, the picture shifts: 152 points served by one carrier vs. 92 served by more than one.

Recent new entrants are tending to follow the "low-fare" format of point-to-point basic service. These include Jetsgo and CanJet with scheduled service. Skyservice/Conquest has introduced a new domestic charter product. New regional entrants have been minimal. With the exception of Hawkair in British Columbia, the others have had little impact on the national competitive picture, and one, Bay Chaleur, has ceased operation.

What the Future May Hold

Whatever the future looks like, it will look very different from today. Westjet is considering expansion into the US market within the next few years, and hopes to do so in cooperation with a U.S. partner. This would provide low-fare transborder service to Canadians on a scheduled, year-round basis, and provide a Canadian competitor to Air Canada's transborder business.

A second major shift is the unsurprising distaste that most carriers now have for mergers and acquisitions. As Air Canada discovered, they are emotional, expensive and messy. Domestic carriers in the United States seem to be shifting to the alliance model, in which a number of airlines come together, code share, honour each other's point programs, etc. This scheme has already been adopted by UAL and US Airways, and would allow them to book and connect passengers on one another's flights, codeshare and redeem each other's frequent flyer miles. This agreement, which involves no equity exchange and sees both airlines remain separate companies, is a far cry from, and a far less risky move than their failed attempt at a merger two years ago. Depending on how the Canadian industry evolves, similar agreements could be expected here.

The third change is one that we have seen Air Canada take, which is the "boutiquing" of airline products. From a full-service, high-cost airline, Air Canada is attempting to develop products that will meet the needs of all travellers: low-fare point-to-

point (Tango), high-end (Jetz), low-cost networked (Zip) and full-service and regional network (AC mainline and Jazz). Only time will tell if the strategic shift from a bum for every seat (yield management) to the new paradigm, a seat for every bum (niche products) will work, but trying to meet new demand with only high-end products clearly won't.

A note about the numbers:

There are several ways that the size of the airline industry can be measured. This report generally uses a standard method, seat-kilometre. While this measurement only portrays a partial picture, it is a relatively straightforward way of describing the airline industry, and provides insight into how the airline industry is shaping up. Where further detail is useful, such as in the domestic services, the number of seats flown is also used as a point of comparison.

Unless otherwise noted, Air Policy, Transport Canada provided the data quoted in this report, using statistics from Back Associates Official Airline Guide. Every effort has been made to ensure accuracy, and any errors are my own.

What Should Government Be Doing About the Airline Industry for the Long-term?

Air Policy

Current Canadian air policy rests on four pillars: Canadian ownership, reciprocal bilateral agreements for international scheduled service, domestic deregulation and a shift to user-pay systems. This section examines the impact of these policies on the government goals of efficiency, viability, affordability, and domestic and international competition.

Canadian Ownership: Is Made IN Canada also Made FOR Canada?

Currently, the freedom of Canada's skies does not extend to foreign-owned carriers. Airlines must be 75% owned and controlled by Canadians. There is some rationale for this. States, including Canada, negotiate bilateral air agreements on behalf of their national carriers. Canadian-owned companies provide high quality jobs, head offices, and businesses that have a good knowledge of, and a special interest in the success of, the Canadian market.

It has been assumed by the current government that Canadian-owned airlines offer a greater good for Canadians, and that the intrusion of foreign carriers or foreign ownership would destabilize the Canadian-owned system, and most importantly, leave Canada with an essential part of its transportation network in the indifferent hands of non-Canadians.

There are a number of reasons that the government supports the "made in Canada" option. Canadian airlines view the Canadian market as their opportunity to increase investor value. The better they serve Canadians, the better their return. Canadian airlines employed 83,000 people in 2000³. Foreign carriers flitting in and out of the Canadian market could damage existing carriers, de-stabilize the market and put airline employees at risk. This leads to the nightmare scenario of weak Canadian airlines, no investor interest, and no carriers, foreign or domestic, adequately serving Canada's needs, particularly in more remote or rural regions.

In this light, the "made in Canada" policy may be seen as the best of all worlds: Canadians controlling their own airlines, with the inherent benefits of high quality jobs, head offices, and decision-making that is at least influenced by national considerations. In this way, we do not leave our important air connections and the \$4.2 billion airline sector⁴ to the vagaries of foreign carriers.

³ *Transportation in Canada 2001 Annual Report*, Transport Canada

⁴ *Transportation in Canada 2001 Annual Report*, Transport Canada

However, Canadian-ownership should not be considered a dogmatic good. Obviously, a “made in Canada” policy is good for Canadian carriers. But does it lead to greater efficiency or viability? Does it lead to stronger competition? Most important, is it good for Canada?

For most other sectors, the government answer is an open market is better for Canada than a closed one. For example, the North American Free Trade Agreement (NAFTA) has provided the following benefits:

Under the NAFTA, Canadian producers are better able to realize their full potential by operating in a larger, more integrated and efficient North American economy...Consumers benefit from this heightened competition and integrated marketplace with better prices, greater choice of products and higher-quality goods and services.⁵

This begs the question: if open markets provide all these benefits, why would they not apply to commercial aviation?

The term “made in Canada” or “Canadian-owned”, implies that Canadian carriers’ business practices and decisions somehow encompass broad national interests as well as their own self-motivated interests. However, in a de-regulated environment, government has little control or involvement in decisions made by airlines and cannot use the carriers as a tool of economic or social policy.

There is absolutely no onus on our airlines to serve a greater good. They do not have to serve communities if they do not wish to do so. They do not have to set prices in a way to encourage travel by Canadians. They do not have to “buy Canadian”. Their “masters” are not the Canadian people, or our common goals, but the marketplace, shareholders and customers. The Maple Leaf on the tail of an Air Canada plane is not a symbol of national identity. It is a corporate logo.

“Made in Canada” suggests an outcome that cannot be fulfilled – a societal benefit bestowed on the collective by a private-sector industry. Consequently, when carriers, especially Air Canada, fail to deliver on “Canadian” goals, people feel betrayed.

This unrealistic expectation would disappear if we shift airline policy towards the same principles that guide NAFTA and other free trade agreements, such as the General Agreement on Trade in Services (GATS): a “made FOR Canada” rather than a “made IN Canada” policy.

A “made for Canada” policy implies that air travel is a means to an end, and that end is much more important than the carrier sector itself. “Made for Canada” says that just being homegrown isn’t enough. You also have to be good. Nationality and ownership are subsumed by the requirement to deliver an excellent product, based not on where you live, but what you can do.

⁵ Department of Foreign Affairs and International Trade Web site: NAFTA overview

What do we risk? From an economic point of view, in 2001, air travel generated 0.4 per cent of the GDP. **All** purchased commercial transportation; of which air is only one element generated 1.5% of GDP⁶. Its relatively small size suggests that the impact that the airline sector has on our economy is far larger than the size of the airline sector itself: for a small dog, it has a big bark.

There are four specific risks associated with an open market. The first is to Canadian carriers who could fail. The second is to Canadians who would be at the “mercy” of global market forces. The third risk is the loss of “sovereignty” of Canada’s airline industry. The fourth issue is almost more of a question of timing than a risk. What happens if we open our country to foreign carriers, and none come in?

These challenges are not as overwhelming as they first appear. We already live with many of those uncertainties. Canadian carriers have already failed. We are, and have been, at the “mercy” of market forces ever since the airline industry was deregulated. Other than Air Canada, which was required to serve all communities served by AC, Canadian Airlines Corporation (CAC) and their regional carriers, for a three-year period that ends this year, carriers have left (and entered) routes routinely for over a decade. Canadian airlines serve communities if the economic argument makes sense; rarely, if ever, as a matter of civic pride.

The concern that foreign carriers would substantially weaken our existing airlines ignores the natural advantage Canadian carriers have, and would continue to enjoy even in a more open regime. They know the market. Their brands are established. Their distribution channels are well entrenched.

A fear often expressed is that the “made-in-Canada” airline solution protects Canadians from foreign carriers that would “cherry pick” the best routes, leaving marginal money-losers behind. This argument fails. Air Canada is serving “beyond the gateways” destinations in order to build network feed or because the route makes money on its own. One can assume that any other network carrier would need regional feed for the same reasons. The business case for developing a strong network or point-to-point system is equally valid for both Canadian and non-Canadian carriers.

The issue of sovereignty is perhaps the most serious, because it is emotionally charged. In two years of examining this issue, the views I have heard on Canadian ownership are more a matter of ideology than fact. One either believes that global trade strategies employed in other sectors would work in the airline industry or one believes that the country is better served from within. For the reasons stated earlier in this section, I believe the needs of Canadian sovereignty are better served by a

⁶ *Transportation in Canada 2001 Annual Report*, Transport Canada

policy that is made **for** Canada. Protecting private-sector companies simply because they are owned by Canadian citizens does not necessarily achieve that end.

Another “risk” is that even after liberalizing the environment, no foreign carriers would step into the Canadian market. However there is a difference between a market-place response and government policy. The former merely reflects what corporations do. The latter determines the rules of the game by which corporations act and compete. It is not the role of government to increase competition. It is the role of government to establish the environment, and let the realities of the market play out, within the rules that government believes are in the best interests of the country. If the government were to shift its policy tomorrow, it would still take years to feel the effect of the change.

Building Competition: Not If, but When

The status quo strives to maintain a balance between protecting a key Canadian industry and allowing competition. In its defence, given the shaky position of many carriers right now, a “wait and see” attitude can be considered prudent. However there is a price to pay for this caution. Long term, if Canada does not commit to liberalization quickly, it loses not only time, but given the fluid global environment, may be forced to react to other countries’ initiatives, rather than set its own “free trade in air services” agenda. A short-term delay would be more palatable if it did not result, as it has, in the continuing dominance of one carrier, and the effect of its size on Canada.

In fact, the spectre of Air Canada’s dominance was of concern when Bill C-26 was drafted. In the government’s formal response to the Standing Committee on Transport Report entitled “Restructuring Canada’s Airline Industry: Fostering competition and protecting the public interest” the Minister of Transport said

*“The Government of Canada is committed to achieving a healthy, Canadian-controlled airline industry. The government’s goal is to foster competition from Canadian carriers. It is doing this by ensuring that the conditions for attracting competition from new and existing carriers are in place. **Should there be competition concerns in the future, the government will consider what other measures may be necessary.**”*

*“In addition, while no talks on these recommendations are currently scheduled with the United States, **the government has not ruled out these options as items for discussion in the future, in the event that there are competition concerns that cannot be addressed by Canadian carriers.** (emphasis mine)”⁷*

⁷ Government Response to the Standing Committee on Transport Report Entitled “Restructuring Canada’s Airline Industry: Fostering Competition and Protecting the Public Interest”, February 17, 2000

The Air Canada Dilemma

Air Canada's importance to Canadians cannot be measured simply by its market share, but also in the fact that it is a key enabler for global and local business, trade and tourism. It is the only carrier in the country which offers internationally allied, full-service carriage, with high frequencies, frequent flyer points and perks and seamless connections to over 800 domestic, transborder and international destinations through its own network and through partnership in Star Alliance. It has a growing stable of services, including the popular but controversial Tango, the newly re-named Jazz regional service and the yet-to-be-launched low-cost carrier, Zip. It is reinventing the way it does business.

In fairness, Air Canada also carries a legacy of its days when it was a Crown Corporation. Even today, fourteen years after it was privatized, considerable numbers of people still think the airline is government-owned, or at least, government-controlled. It is not. However, it still has to adhere to a number of unique government requirements through the Air Canada Public Participation Act. For example, it is the only carrier that is subject to all of the provisions of the Official Languages Act. Until recently, individual ownership of shares in Air Canada was limited to 15%.

Air Canada has been portrayed as arrogant and unresponsive and even characterized by some as an out-and-out bully. While some of this might be true, I think the negative image is exaggerated by the airline's sheer size as well as its burden of history. We hold Air Canada to a different standard. What might be acceptable if it were one competitor among many, is not acceptable when it holds such a large, and relatively undiminished piece of the market.

At the start of "restructuring" in 2000, Air Canada, having newly acquired Canadian Airlines, held about 77% of the market, measured by daily average seat-kilometres⁸. Tellingly, despite everything that has happened in the last year, including the expansion of Westjet and the entrance of new carriers, Air Canada STILL has 73% of the market in 2002. This suggests that the competition may have taken as big a bite out of AC as is possible, and that any other market shifts will be small and incremental. Parenthetically, as a straight-line projection, and assuming no significant market growth, if Air Canada continues to show an average decline in market share of two per cent a year, it would take until 2008 for Air Canada to reach a somewhat more competitive 60% share of market.

If this supposition is correct, Air Canada's dominance, both in absolute size and in products, will continue with little or no change for the near future. The carrier can be expected to reduce its market share by only so much: it cannot shrink its way into

⁸ Domestic Operating Statistics, Schedules Airlines, Daily Averages July 2000, Source: Back Associates Official Airline Guide database, prepared by Transport Canada, July 17, 2001

profitability. In my view, this leads to an untenable situation of too much public reliance on one private carrier.

There are enough immediate concerns about the growth of competition that the government should take further action now to increase competition through a more liberalized regime rather than wait for optimal conditions.

Policy at a Crossroad

Will Canadian carriers be able to overcome Air Canada's dominance with no change to current policy? We are at a crossroad. One road "plays it safe" and hopes that the airline industry will eventually evolve into one that balances our reliance on Air Canada with a wider availability of choice of other Canadian carriers. The second road demands action now: a new policy framework to open the aviation market to liberalized trade.

New opportunity is not without jeopardy. It is difficult for any industry to move from a protected to an open market. Some carriers may weaken or not survive the transition. Who survives, who thrives, and who fails will be up to consumer choice and carriers' ability to adapt to the new market. The potential of great success comes only with great risk.

Building a new policy framework

If liberalization is the best approach for Canada, the next question is what is the best strategy to achieve it? There are two different ways. The first is to liberalize current agreements incrementally, small step by small step. The second, and to my mind, far better approach is to start with a fresh canvas and create a new policy framework that serves Canada's interests first and sets an innovative and far-reaching agenda for air service.

Domestic and International Liberalization: Two Sides of the Same Coin

Canada currently distinguishes between "domestic" policy, which can be decided by the federal government acting alone, and "international" policy, which requires international agreement. Since passengers do not fly policy rubrics, but to their destination, there is considerable overlap in the real world between "domestic" and "international" air service.

The domestic market supports the international market and vice versa. In a world that is shrinking to the point that one can do business in one country and live in another, or an individual is as likely to visit relatives in Hong Kong as in Regina, the distinctions between "domestic" and "international" are becoming artificial and irrelevant. For this reason, liberalization options are reviewed in the following section as a continuum rather than a subset of either domestic or international policy.

What Should Be on the Table?

Every avenue of liberalization should be explored within a new policy framework. Changes can range from very significant: foreign ownership of Canadian carriers, to the relatively small: extending the right for foreign carriers to carry domestic traffic (cabotage). The key is not whether the changes are large or small, but whether they serve Canadian goals.

Routes to Liberalization: Foreign ownership

One way to enhance the potential of competition is to allow foreign ownership of Canadian carriers. Also known as “right of establishment” or “commercial presence”, this ownership model requires in-Canada management and results in investment in Canada: headquarters, jobs, etc. Equally, this option would also allow foreign carriers to purchase a controlling share of a domestic carrier. However, a foreign-owned domestic carrier is not a complete match for Air Canada. A foreign-owned in-Canada airline would likely not be granted international routes by Canada, both because of current law which forbids it and because it may not be acceptable by the bilateral partner. However, it would be possible to interline or code share with other international airlines, providing an alternative to Air Canada and Star Alliance.

A domestically operated carrier, regardless of ownership, brings many fundamental benefits to Canada. The company and its employees would pay Canadian taxes and live (and spend) in our communities. It is true that decisions would be made on business, not social strategies but that is true already of Canadian carriers and, indeed, private Canadian businesses generally.

Another potential benefit is to third-tier carriers who wish to feed into a network system. A foreign-owned domestic airline that has international links, would likely be interested in developing regional feed. This could increase competitive opportunities on regional routes, and provide smaller carriers with a partnership other than Air Canada/Star Alliance.

Another, less radical, avenue is to increase the foreign ownership provision from 25% to 49%. Some believe that this would have a positive effect on Canadian carriers' ability to increase investment and build alliances. Others worry that this is a back door to control of Canadian carriers. Most likely, this provision would make little difference initially, but could provide some new options and opportunities in the future.

Routes to Liberalization: Enhanced Bilateral Agreements

As an interim step, the government may choose to keep the rules of ownership intact, and expand competitive options by liberalizing current bilateral agreements. While this approach does not bring the potential benefits to Canada of head offices or jobs, it can move the airline sector into a more contemporary trade environment relatively quickly.

International passenger air service is governed by bilateral, government-to-government negotiations of traffic rights. The level of restriction or liberalization of each of the 70-some agreements signed by Canada varies widely. Canada has displayed a consistent, though cautious, trend to more liberalized agreements.

The hallmark of the bilaterals is their symmetry and the fact that they are based, to a significant degree, on carriers' international strategies. If Canada is negotiating with a restrictive regime, the final agreement will likewise be fairly restrictive as well.

A country will enter into negotiations because one (or more) of its international carriers is interested in that market. With some exceptions, Canada will not allow foreign carriers more freedom in Canada than that foreign government is willing to give to Canadian carriers in its home country, in effect ensuring that negotiations consider the interests of Canadian carriers.

However, as early as 1994, the Canadian government recognized that there was a larger "community of interest" that had a stake in the negotiated outcomes. In the 1994 document, **Canada's International Air Policy**⁹, the government stated

"The particular role and challenge of government is to formulate a clear and coherent set of objectives, strategies and policies that meet the overall national interest. The following objectives for a Canadian international air policy are established as being in the broad national interest:

- *To provide better international air service for Canadians*
- *To support our international trade, business and tourism objectives*
- *To respond to the needs of airport and export communities*
- *To ensure consumers are protected and have all the necessary information to make the travel choices best suited to their needs.*
- *To create a growth-oriented environment for the air industry"*

In the same document, the government allowed, for the first time, limited foreign carrier access even if Canadian carriers were not interested in serving that foreign market in return. These rights were limited to two flights a week and excluded Toronto. Icelandair was the only carrier to take advantage of this option, flying to Halifax, and after several years of lobbying by Icelandair and the Halifax region, was permitted an additional 3 flights a week, (with two able to fly to Montréal or Winnipeg). However, Icelandair soon left the Canadian market. Some have suggested the limit of two flights a week virtually guaranteed failure, and that this

⁹ Canada's International Air Policy, TP12276, December 1994,

provision did not go far enough to respond to consumer interests, favouring instead the interests of Canadian carriers in general and Air Canada specifically. The additional flight options were a case of “too little, too late”.

However, this is a useful example of how the Government of Canada granted traffic rights to a foreign carrier and served a broader interest. The Iceland service may not have done much for Canadian carriers, but it brought thousands of people into Halifax, not only as tourists, but also as purchasers of a wide array of high-end Canadian goods.

In 2001, the government began a review of its 1994 policy, and a detailed discussion paper was released in April of that year, acknowledging

“While in the past Canada’s negotiating approach focused on the interests of Canada’s primary carriers, efforts are now being made to balance the interests of airlines, airports, Canadian communities and consumers, on a case by case basis. With these interests in mind, Canada increasingly negotiates bilateral agreements that feature a broader exchange of rights and less regulation than before. The broader service opportunities and decreased government oversight of carriers’ commercial choices are designed to foster more competitive and efficient markets.”¹⁰

In the same document, the government also acknowledged

“...administering a new international air policy would be easier and less controversial if its objectives recognized the need to move towards increased liberalization and clarified how a balance between the interests of all stakeholders could be achieved.”

Unfortunately, the follow up to the consultation process was delayed in the aftermath of September 11th. Other than a recent announcement (May 2002), which now allows all Canadian carriers to apply to operate scheduled international services, regardless of the size of air travel markets, the government has stated that

“other issues raised, such as the liberalization of Canada’s approach to bilateral air negotiations, will be reconsidered when the Canadian airline industry has more fully recovered from the recent economic downturn and the events of September 11, 2001”¹¹.

In practical terms, it is likely that Air Transat is the only carrier in a position to take advantage of the new policy. More worrisome, we do not know how long it will take the airline industry to recover (or exactly what “recovery” means in this context). If the government is waiting for ideal conditions, there could be a long wait before we pursue a policy that balances all stakeholder needs and allows for a more liberalized regime.

¹⁰ Canada’s Policy for International Scheduled Air Services: Issues for Discussion, 2001

¹¹ Transport Canada News Release, No. H051/02, May 21, 2002 **Transport Minister Announces New Policy for International Scheduled Air Service**

Route to Liberalization: Open Skies

The bilaterals have a lot of latitude in how far liberalization between two countries can go. For example, since 1995, Canada and the United States have had an "Open Skies" agreement. All Canadian and U.S. carriers are authorized to operate on any and all transborder routes, without restriction. However, cabotage, or the right of foreign carriers to carry domestic traffic, is not permitted.

Even with that limitation, transborder traffic grew from 13.6 million passengers in 1994 to almost 20 million in 1999¹². Transborder service grew from a total of 136 city pairs served in 1996 to 186 in 1999. Both Canadian and U.S. carriers benefited. In 1995 there were 70 Canadian carriers and 66 U.S. carriers serving transborder city pairs. In 1999, the numbers grew to 96 Canadian and 90 U.S.¹³ Although the Canada – U.S. transborder market may be unique in some ways, there may be equivalent benefits if similar, or even more liberalized agreements were instituted with other countries. Equally, Canada and the United States may extend their current version of "Open Skies" to include cabotage.

However, incremental liberalization, such as allowing foreign carriers cabotage rights, is of limited use unless it is made within a broader context of liberalized air trade policy.

Route to Liberalization: Multilateral Options

While the airline industry still negotiates bilaterally, the rest of the economy seems to be moving to a "borderless" world for commerce, through regional mechanisms such as NAFTA or global ones, such as the General Agreement on Trade in Services (GATS).

In recent years, there has been an acknowledgement that the airline industry is behind the times, and there has been a movement to multilateral accords. The European Union now has a "common aviation area" that allows for cross-border airline mergers and takeovers and permits airlines from one member state to set up operating subsidiaries in other member states. The U.S. government has a multilateral Open Skies agreement with four Asia Pacific nations.

The Canadian government seems to be taking a more serious view of multilateral options, and has recently released a consultation paper on air transportation services within GATS, which invites comment and input on the desirability of including a wider range of air transportation services and states:

"the present exclusion of air traffic rights and services associated with exercising these rights (i.e. including scheduled and unscheduled air services, air navigation and airport operations) will be reviewed. Members will examine possible ways of applying the GATS

¹² Source: Canadian Transportation Act Review, Vision and Balance, June 2001

¹³ Transport Canada, Air Policy

to air carriage. If major changes are implemented, this could imply the progressive abandonment of the present bilateral framework¹⁴."

As well, groups are beginning to look at "common aviation areas" for other regions of the world. A concept has been advanced to consider the formation of a Transatlantic Common Aviation Area (TCAA) between the United States and Europe, which has been promoted by the Association of European Airlines (AEA)¹⁵.

While a TCAA is a long way from reality, it would be worthwhile to review the pros and cons of the scheme, from the Canadian perspective, to see if it is worth serious effort or promotion on our part. As the Canada Transportation Act Review Panel noted, even though there was little support at this stage for a TCAA, "*Canada cannot afford to be left out of a future accord, given its strong links to the U.S. and some EU members.*"¹⁶

Route to Liberalization: Balancing benefits for carriers and Canadians

Canada has the freedom to act unilaterally when it is clearly in the interest of Canadians. However, in practice unilateral action is controversial. Trade liberalization benefits Canadians because it works in two ways: it offers more consumer choice, and it allows Canadian business to expand into larger, international markets. The expansion of Canadian businesses internationally leads to more jobs here at home.

In principle, I support reciprocal agreements. They are more equitable to the business sector being affected. They provide Canadian negotiators with more "ammunition". They enhance business opportunities for Canadian companies. In an ideal world, all liberalization agreements would be symmetrical.

As important as reciprocity is, it is not the entire story. We cannot measure the value to Canada of the airline industry only by the number of tickets it sells. Airlines do more than provide transportation. They also enable the growth of other business sectors. Since Icelandair's inaugural flight in 1996, Icelandair helped to generate over \$14 million in tourism revenues for Nova Scotia, according to the government of Nova Scotia. The numbers do not stop there. In 2001, foreign travellers to Canada generated more than **\$14 billion** in accommodations, food and beverage, retail and other commodities.¹⁷ This spending impacts directly on communities across Canada, in businesses large and small.

¹⁴ Services 2000 Air Transportation Services, A Consultation Paper in preparation for World Trade Organization (WTO) General agreement on Trade in Services (GATS) Negotiations, prepared by Transport Canada

¹⁵ Towards A Transatlantic Common Aviation Area, AEA,
http://www.aea.be/Topics&Views/FramePage_topics.htm

¹⁶ Source: *Vision and Balance*, Report of the Canadian Transportation Act Review Panel, June 2001

¹⁷ National Tourism Indicators, System of National Accounts, Statistics Canada, First Quarter Estimates, 2002, catalogue # 10-009-XIB

This leads to a concept of a trade in benefits for Canadians rather than a trade in benefits for carriers. The government has already recognized the need to include a broader “community of interests” within the context of international air negotiations and to balance those interests with those of Canadian carriers. This inclusion may lead to unilateral action by Canada on occasion: when the benefits of the “value” trade are obvious for consumers, for example, and either have no impact on the carrier industry, or when the carrier interests are clearly subsumed by a greater benefit.

Another reason that Canada should have an option of unilateral action would be if the carrier community were able to wield too much control over the government’s trade agenda. The government must be free at all times to negotiate agreements that would benefit Canadians, regardless if the Canadian airline sector was on-board or not in the short-term. For example, I believe that the Government of Canada negotiated the 1995 U.S. Open Skies agreement without a great deal of airline support in the early days. It would be unfortunate if similar opportunities would be missed simply because too much emphasis was put onto the immediate business strategies of airlines and not the long term and broader implications for consumers and for Canadians.

With Whom Should We Negotiate for Liberalized Air Access?

We should look first to the United States, our biggest trading partner and the largest market for air services in the world. It will not be an easy process though, as the U.S. has similar restrictions as Canada on foreign ownership and foreign carriers flying U.S. domestic routes. There has been little to suggest that this policy is being reviewed by the U.S. government. However, this might change as at least one major carrier, American Airlines, has publicly called for a more open trade agreement in air services between Canada and the United States. Don Carty, President and CEO of AMR (and former President of Canadian Airlines International) recently said, in a speech to the Vancouver Board of Trade,

“In a traditional context, David Collenette, the federal Transport Minister, was correct when he recently asserted that U.S. carriers would balk at the notion of abolishing limits on cross-border ownership, and allowing reciprocal cabotage...But there has been a shift in opinion, and I believe there is a rapidly emerging consensus among U.S. airlines that we ought to fully liberalize commercial aviation between our two countries – notwithstanding the fact that it will mean more competition for us. Such a complete liberalization will not only facilitate more service and even more trade between our countries, it will also inject much-needed competition into lots of domestic markets¹⁸”

Hopefully, Mr. Carty’s comments will herald the start of an innovative and progressive agenda, and will help lay the foundation for a new and more liberalized agreement between our countries.

¹⁸ Remarks of Don Carty Chairman and CEO, AMR, Vancouver Board of Trade, June 27, 2002,

As important as the United States is, it is not our only trading partner. For example, Canada should also negotiate freedoms with the E.U. common aviation market and with our key Asia Pacific trading partners as well as other countries as they serve the interests of Canadian.

1.0 Air Policy Recommendations – Liberalization

General:

- 1.1 That the Government of Canada create a new “made for Canada” policy framework to fully liberalize the competitive marketplace for air service to and within Canada, that serves to create an efficient and viable airline industry with strong domestic and international competitors and satisfies the needs of all Canadians.**
- 1.2 That the government make every effort to reach reciprocal agreements, but be prepared to liberalize air service without direct or immediate reciprocal benefits for carriers, if there is an obvious advantage for Canadians and consumers, and when the liberalization has either no impact on the carrier industry, or when the carrier interests are clearly subsumed by a greater benefit.**

Foreign ownership:

- 1.3 That the Government of Canada liberalize the current rules of ownership to allow foreign-ownership of domestic Canadian carriers and a 49% ownership level of international carriers.**

International Liberalization:

- 1.4 That the Government of Canada rigorously pursue and accelerate a program of liberalization under the bilateral regime.**
- 1.5 That the Government of Canada work to achieve liberalized air agreements with key multinational partners and plan towards the establishment of common aviation areas.**

Domestic deregulation

Through a series of steps between 1970 and 1988, the government moved from total regulation of the domestic airline industry to complete economic deregulation, retaining regulation of safety matters. Prior to deregulation, the Canadian government controlled whether new carriers could enter the market, where carriers could (and

could not) fly and how much (or how little) carriers could charge their customers. Air Canada was a Crown corporation, under federal control.

Consumers had no direct role in determining their level of service or influencing price. Those were determined in Ottawa, in hearings conducted by a government regulatory body. As the civil aviation industry matured and demand increased, government regulation, rather than protecting consumers, seemed to serve only to buffer carriers from the realities of the marketplace. The government found itself in a no-win situation, second-guessing a rapidly changing market, using a very poor tool: a slow and complicated bureaucratic process.

Deregulation was intended to allow carriers themselves to respond to the market directly, without prior government approval and to move price and purchase decisions into the hands of the people directly involved in the transaction: the airlines and their customers. Deregulation, does not, despite the claims of its more enthusiastic supporters, axiomatically result in lower fares and more choice. It does, however, make those goals much more achievable than would be possible in a regulated environment.

Today, airlines watch the market, not the regulators. Carriers go where they can make money, a complicated decision that involves not only the level of demand, but internal costs, the type of equipment available to serve the route, competitors on that route and other factors. It is increasingly unlikely, and inappropriate, to expect that any carrier, including Air Canada, would fly routes that lose money.

Deregulation has made it easier for carriers to enter the market, and offer exactly what consumers want at the moment. Today that happens to be no-frills, low-fare travel, currently at 36% of the market and climbing.

Canada 3000 that had about 11% of domestic capacity by seat-kilometre in July 2001, has been replaced, in less than one year, by WestJet, Air Transat, Air Canada's Tango and the newest entrants into our skies: Skyservice/Conquest flying as a domestic charter and two new scheduled carriers, Jetsgo and CanJet.

While there are many benefits to a deregulated airline industry, this economic freedom is not free. New opportunity also means new and higher risk. Carriers are not sheltered from aggressive competition, only from overt predators. Weak business plans or management errors are exposed quickly and sometimes fatally. There is no government backstop, and carriers are on their own to survive in a highly complex and volatile market. Most significantly for smaller communities, deregulation allows carriers to leave a market if the economics make no sense – leaving some, potentially, with no air service at all. Deregulation also prevents government from using air access as a tool of economic or social policy. Moreover, any thought that deregulation would lead to a permanent state of full competition for all regions has been rejected by the marketplace itself.

Because we have not seen the development of full competition, some see deregulation as a failure. Competitive services have grown, but Air Canada still flies three out of every four kilometres in Canada. Air Canada dominates, yet it is not obliged to serve Canadians except where it chooses. Still, Canadians rely overwhelmingly on Air Canada to connect them to other communities and countries. Some advocate that the government either force Air Canada to release capacity to other carriers or reconstitute it as a controllable Crown corporation.

I believe these actions would ultimately fail Canadians. We eliminated economic regulation because the airline industry had matured beyond the need for paternalistic oversight from Ottawa. Near the end of the regulated era, the process to set rates, routes and capacity became onerous. The standing joke was that the only people who gained were the army of lawyers employed by carriers to make their case to the Canadian Transport Commission.

Based on experience, government regulation of the airline industry breeds inefficiencies, is slow, overly interventionist and takes the power of choice from consumers' hands. It also removes the incentive for carriers to innovate, to improve or compete. In the real world, the airline sector is extremely fluid. Carriers have to be ingenious, take risks, lower costs and increase revenues. Re-regulation would impose a static environment, which would likely provide a minimum level of costly, mediocre service.

Secondly, there is no guarantee that even with the most draconian of government intervention, Canadians would be better served. Decisions could be made based on short-term political rather than long-term policy goals. It is a slippery and subjective slope from government intervention to government meddling. Rather than deal with airlines directly, Canadians would be subjected to the "whims" of government regulatory bodies. Thirdly, regulation is no guarantee of any airline's success. Carriers could still fail or require government bailouts, and communities might be left without service even under a regulated regime.

Finally, the world has changed in the last 30 years. The re-regulation of Canada's airline industry, in my view, represents a giant step backwards. It would say that Canadians are too feeble to support an independent airline sector by virtue of their consumer power; that we are overwhelmed by our geography and that we can only get air service if our government gives it to us. I find these arguments specious and insulting.

First, most Canadians are anything but isolated and remote. The most recent Statistics Canada census figures show almost 80% of Canadians live in urban centres of 10,000 or more and, 51% live in one of four major urban regions: the B.C. Lower Mainland and southern Vancouver Island; the Calgary-Edmonton corridor; the extended "Golden Horseshoe" in southern Ontario and Montréal and its adjacent region. It is estimated that over 80% of Canadians are within two hours of an airport with scheduled service. With the possible exception of some northern and other re-

remote communities, we have, for the most part, overcome our geographical destiny and our need to build our nation through east-west transportation links. The notion that the Canadian demand for airline service is so weak that carriers wouldn't be interested in many markets is equally hard to credit.

Compared with other nations, Canadians are a peripatetic group, ranking seventh in the world in passenger-kilometres flown, seventh in passengers per capita and fourth in both passenger-kilometres per capita and passenger-kilometres per \$1000 GDP¹⁹. In 2001, Canadians spent a very significant amount – \$12.6 billion – on passenger air transportation²⁰.

While these data do not tell the entire story, they do support the contention that Canadians generally are urban consumers, who, despite the size of the country and the small population, spend a significant amount for passenger air services and fly in significant numbers, even in comparison to other countries.

This pro-deregulation position does not ignore the problems yet to be solved, or that have been caused, by deregulation. It simply posits that deregulation is, on balance, a more useful tool overall for Canadians than a regulated regime. The issues that are exposed by deregulation: service to small and remote communities, instability in the marketplace and the continued dominance of Air Canada can be addressed more effectively by other means. These recommendations are found in other sections of this report.

2.0 Air Policy Recommendation: Deregulation

- 2.1 That the Government of Canada continue to pursue its policy of domestic deregulation, and not re-regulate the airline sector in general or Air Canada in particular, and that it seek to deal with issues arising out of a market-driven environment by other and more effective means.**

Should the government “stabilize” the airline industry?

The airline industry is, and has been, highly unstable. Carriers have left passengers stranded. Employees have lost their jobs. Airlines have been created and almost as quickly, disappeared. This breeds an uncertain environment not only for airlines, their employees and their passengers, but also for business, especially tourism, and

¹⁹ Sources: Air Traffic – ICAO Statistical Yearbook; Population: DRI_WEFA, GDP:OECD, information provided by Transport Canada

²⁰ Statistic Canada System of National Accounts, National Tourism Indicators, Quarterly Estimates 2001, Catalogue no. 13-009-XIB

for investors. As a result, some have called for the creation of a government stability program for carriers.

However, there are some problems with this idea, beginning with the false sense of security it engenders. The American government instituted a \$10 billion loan guarantee program post-September 11th. Even with this, there are no guarantees and there is speculation that at least one U.S. carrier will go into "Chapter 11" in the next few weeks. If there is one, chances are there will be more.

Although the government and Minister were subject to harsh criticism when Canada 3000 declared bankruptcy, I think their approach was correct, albeit unpopular with some groups. Tossing money at a crippled business tends to mask the illness, not cure it, analogous to treating a broken leg with painkillers when it needs a cast. Arguably, if Air Canada was given the protection it sought publicly in the days following September 11th, it would have had no incentive to institute the sweeping reforms to its costs structure and product line. There would be no "new" and improved" Air Canada, just one that was "the same old, same old", relying on government to make the pain go away.

The government rightly imposed strict requirements on Canada 3000, even if it meant the temporary retrenchment of its own "made in Canada" competitive solution. Tax money given to private companies should come with stringent requirements, and return a benefit to Canadians. The government's best action would be proactive, not reactive. It should ensure that the environment is right for start-ups; that entrance requirements are neither too stringent nor too lax; that carriers have reasonable access to capital; that the user-costs associated with air service are not making the mode uncompetitive; that the economy is growing. In other words, any action taken by government that contributes to the health of the economy and the airline industry will lead to a more stable sector, without the need for special bailout programs. Direct government assistance should only be considered in extraordinary circumstances. Government should step in only after all other avenues have been explored, and even then, to shield Canadians, not businesses, from harm.

User pay, user benefit?

For more than 30 years, the Government of Canada has pursued a course of commercialization of transportation, first articulated by the 1961 MacPherson Commission.

This was one of the underlying concepts behind deregulation, and the move to greater reliance on marketplace forces. Part of the process was the devolution of air infrastructure facilities (i.e. airports) and the introduction of user fees, some of which were driven not only by policy, but also by the government's need to control spending and reduce its deficit and debt. Today, the Government of Canada has devolved most commercial airline related costs to the users of the air system: airlines,

airports, and of course, passengers. These imposed fees, as well as existing taxes, have an impact on how much people are asked to pay and, if too unreasonable, may impact levels of consumer demand, airport viability and the level and type of domestic competition in the market.

While a “user-pay” policy makes economic sense overall, there are three issues that have been exposed, and remain unresolved, by this policy. These relate to the government’s stated goals of an airline industry that is affordable and responsive to users and their communities. These are:

- One, how can we manage and publicize the number of fees, charges and taxes in a transparent and fair way, so that passengers are aware of the total price of air travel prior to purchase?
- Two, are there sufficient mechanisms to ensure that user fees and taxes are applied in a fair and transparent way?
- Three, after following a user-pay policy for a number of years, has the time come for the Government of Canada to review the combined impact and appropriateness of all its user-fees and taxes?

Ensuring User Fees are Fair and Transparent

The “Air Travellers Security Charge” seems to be the proverbial “straw that broke the camel’s back”. It has created a public storm not only about that particular charge, but about all the fees applied to the base fare of an airline ticket. WestJet highlighted the impact with its audacious, and pointed promotion “Ridiculous Fares, Ridiculous Fees”, that showed a special \$6.00 round-trip ticket price exploded to over \$80.00 in real cost to consumers because of fees, taxes and charges.

There are two issues involved with these charges: one concerns the quantity, cost and accountability. The second is the fairness of the process by which customers are informed that fees apply and how much they add to the price of a ticket.

Currently, there are the following costs added to most or all tickets:

Governments add:

- The federal Air Travellers Security Charge (\$12.00 per one way-trip in North America)
- Federal Goods and Services Tax
- Some provinces add sales tax or Harmonized Sales Tax, as applicable

Airlines add:

- NavCan fees (This is not a direct charge to passengers, but to airlines. However, most airlines break this out of their base fee and show it separately)
- Some carriers add a fuel surcharge
- With some exceptions, an insurance surcharge has been added to help defray the increased costs of aviation insurance

Some airports add

- An Airport Improvement Fee or passenger facilitation fee, charged either on the ticket, or on-site at the airport

Some travel agents add

- Service fees charged to customers as airline-paid commissions at times no longer cover the cost of ticket issuance

The problem is made worse as the add-on costs are not publicized in advertisements, and it is often only when the potential customer begins the purchase process that these fees are detailed. To add to the complexity, while some of these costs are quite justifiably broken out of the price of the ticket, such as the legal requirement to show the GST/HST, others seem to be broken out only to make the base price seem lower than it really is. For example, one can assume that fuel charges are part of the cost of flying. Is there any adequate control over what a carrier shows as a “fuel surcharge” as opposed to the cost of fuel imbedded in the price of the ticket? The same allegation has been made by NavCanada on its air traffic control fees charged to airlines but expressed as a passenger fee on the ticket.

Each fee-collector vehemently defends its charge, with some justification. However, this ignores the cumulative impact. Ultimately all these charges come out of only one pocket: the passenger’s. The airlines do not want to be “blamed” for the charges that are not theirs, and want to see the non-airline fees broken out. This is similar to gasoline retailers that break down the cost of a litre of gasoline, and what per cent goes to governments, at the pump. However, the real cost to drivers, the all-in price per litre, is the one that is prominently displayed on signs and is the one that people care most about.

The opposite is true with airline tickets now. Advertising prominently displays what the carrier considers the “base fare”, putting “fees, charges and taxes apply” in the fine print. It is only when one investigates further either by contacting a travel agent or the carrier, that the additional cost is revealed.

There is a concern that the combined result of sticker shock and the increasingly high number and cost of user fees will turn people away from air travel and to other modes. Short-haul and low-fare travel is especially vulnerable, and while it is too

early to make a definite determination, some data are beginning to support this supposition.

The final issue is more complex, and deals with the appropriateness of government and other user fees. The Air Travellers Security Charge is a case in point. Securing the safety of airplanes and passengers doesn't only protect them: it protects all Canadians from the use of civil aircraft as weapons of mass destruction. It should be remembered that the first attempt on the World Trade Centre in New York used explosives in a van in the WTC parking lot. By the logic of the Air Travellers Security Charge, it would be equally sensible to charge security fees on vans or parking lots. In my view, the emphasis on extraordinary security charges for airline passengers ignores the reality of the threat to all Canadians and imposes an undue and unfair burden on airline passengers.

Airline passengers are not treated as travellers in other modes. If we are travelling a highway, tax dollars have paid for the road, its maintenance and for the police who patrol it. Even toll roads have non-toll twins. As airline passengers, we pay for runways, aprons, police and security. Some of these are in direct charges to passengers, like AIFs or the security fee. Others, like policing, are a cost to the airports, which is passed on to airlines, and is ultimately passed on to passengers.

Recently, the media reported that the government is considering massive injections of funding into transportation infrastructure: \$15 billion for the Trans Canada Highway and \$3 billion for railway upgrades. If these tax-payer funded schemes are implemented, the government would have to institute similar programs for airports as well, or risk the entire air system becoming unviable.

3.0 Air Policy Recommendations: User Fees

- 3.1 That the Government of Canada act to ensure that the "all-in" price of airline travel is clearly and transparently communicated to consumers in advertising and promotional material, whenever possible, and that if certain fees or costs are broken out as separate items, (e.g. GST/HST) that there is clear justification or legal requirement to do so.**
- 3.2 That the government monitor the proliferation and level of all fees, including the Air Traveller Security Charge to assess the cumulative impact of these charges on airline demand, especially short-haul and low-fare travel, and to take corrective action if necessary.**
- 3.3 That the Government of Canada review its user-fee/user pay policies and tax structure imposed on the airline sector to ensure that these policies and charges are consistent with those in other transportation sectors.**

3.4 That the Government of Canada include airport infrastructure in any major transportation infrastructure upgrade and spending program.

National Transportation Policy -- Integrating the modes

"The advantages of a seamless, integrated transportation system are undeniable. Both shippers and carriers benefit when their goods and equipment can be quickly and easily exchanged between the modes. Carriers can gain a competitive advantage by building strategic alliances, which lower costs and extend their reach into new markets, enabling them to serve their customers better. The public is better served when congestion, pollution and the need to expand or replace infrastructure can be avoided by the effective use of intermodal transportation. Travelers also benefit when services blend together to meet their needs in a smooth and effortless manner."²¹

While travellers think of "trips", policy makers think in terms of "modes" – each quite distinct. Given the differences between modes and different jurisdictional regimes, tax structures and regulation between federal, provincial and municipal governments, Canada's overall transportation policy is asymmetrical. This makes comparisons between modes difficult, and increases the challenge of developing a common vision and policy for all modes.

Another issue is the fact that provincial and municipal governments have jurisdiction over large amounts of Canada's transportation network, but there is no overarching framework that allows these governments to plan together.

The Government of Canada is currently finalizing its Transportation Blueprint, a federal strategy to respond to the major challenges that will face Canada's transportation sector over the next decade and beyond . Until it is released, we do not know what the Blueprint will contain, nor how extensive it is. However, it is hoped that that the Blueprint will help establish a national transportation strategy that can serve as a framework for provincial and municipal jurisdictions as well as map the course for federal areas of responsibility. If the Government of Canada can succeed in setting the national, as well as the federal agenda, it would be simpler to achieve the efficiencies of a truly integrated transportation system.

An integrated approach is even more important now that the Government of Canada is considering massive investment in highway and rail infrastructures. Airports are a key part of the overall transportation system infrastructure. A spending program designed to improve Canadians' ability to move within Canada and across borders must consider air as well as road and rail.

²¹ Transport Canada, Creating a Transportation Blueprint, April 2001

4.0 Transportation Policy Recommendation: National Transportation Policy

- 4.1 That the Government of Canada's Transportation Blueprint leads to the development of an integrated, equitably funded transportation system, and provides other jurisdictions the framework and vision to assist their long term planning, and that together, all levels of government work to achieve an efficient, safe, reliable and sustainable transportation system.

Other Government Policy that Affects Transportation

"Canadian communities of all sizes — whether urban or rural, Aboriginal or multicultural — face diverse challenges and have unique needs. The Government of Canada will strive to ensure that, wherever possible, its actions and programs are coordinated to help build local solutions to local challenges."²²

Transportation policy has a clear role that is quite distinct from other areas of government policy. According to the **Transport Canada 2002-2003 Estimates - A Report on Plans and Priorities**, the Transport Canada vision is

"The best transportation system for Canada and Canadians"

and its mission

"To develop and administer policies, regulations and programs for a safe, efficient and environmentally responsible transportation system"

This reflects government thinking as defined by the MacPherson commission report as early as 1961, which stated

"[N]ational policy refers to the broadest goals: achieving a national identity and unity, economic development but accompanied by concepts of equality and justice, social welfare, and so on. Transportation may play a role in reaching these objectives, but the focus of national transportation policy is the health and performance of the national transportation system."²³

Transport Canada does not generally address such policy areas as:

- The role that air access plays in economic development
- The impact of tax policy on air travel demand and cost
- The impact of other government policy on air travel demand and cost

²² Speech from the Throne to Open the First Session of the 37th Parliament of Canada, Jan. 2002

²³ *Vision and Balance*, Report of the Canada Transportation Act Review Panel, June 2001

In other words, issues that deal with the economic and social impacts of air access are not a part of Transport Canada's oversight, but are the responsibility of the government as a whole. This section examines where other government departments, and other governments, may play an effective role in dealing with the social and economic issues raised by airline restructuring.

Air Access and Economic Development

As stated earlier, marketplace mechanisms and deregulation do not solve all our problems. One of the most difficult is the role that air access plays in economic development of our communities, especially remote or rural areas.

A link between development and transportation services was made in the Canada Transportation Act (1996), Section 5, which states in a "declaration" that

"transportation is recognized as a key to regional economic development and that commercial viability of transportation links is balanced with regional economic development objectives so that the potential economic strengths of each region may be realized"

There are a number of problems with this declaration that stop it from being an effective tool of development goals. First, it runs contrary to MacPherson.

Second, the declaration is unclear. What does *"that commercial viability of transportation links is balanced with regional economic development objectives"* mean? These objectives are related, but completely different elements of policy: a non sequitur. The attempt to link one with the other has been a source of confusion which either should be clarified, which I am not sure is possible, or eliminated.

Some communities cited the Canada Transportation Act Section 5 declaration as an indication that the Government of Canada is obliged to subsidize air service to assure that "regional economic development objectives" are met. These communities have learned that this argument gets them nowhere.

Much of the discussion around air service in the last two years has centred on why air access is important to achieve economic goals. Intuitively, we believe that increased air capacity and lower fares lead to greater opportunities to expand tourism, attract new businesses and enhance residents' quality of life. Communities that are lucky enough to have good air access have an advantage over those that do not. However, there is little data that qualifies that advantage or considers air service within a multi-modal framework. Common sense suggests that a community that has excellent surface infrastructure would have less of a reliance on air than one that does not.

Despite the gaps in our hard knowledge, air access remains, at least anecdotally, a key element of development. There are four ways that the government may be involved in air access as it relates to economic development. It can

- Create an “integrated” approach, and incorporate air access strategies into existing or newly created regional development programs
- Enhance opportunities for the creation of third-tier independent carriers
- Introduce an “essential air services” program, modeled after the U.S. or similar programs
- Let the marketplace evolve on its own

Integrated Approaches to Air Access

Economic development relies on a number of interconnected building blocks, of which transportation is only one. Communities need a “recipe” to grow that includes good schools, good municipal infrastructure, reasonable (or competitive) municipal taxes, a skilled workforce, and of course, transportation links. But transportation is only one element. Ignoring the other, equally important, ingredients is akin to baking a cake using only some flour, and ignoring the eggs and the sugar. It cannot be done.

As stated earlier, the awkwardly worded Section 5 of the CTA seems to be the only direct link between transportation and regional development, and is an unhelpful one at that. A more useful approach would be to move the government’s “social welfare” obligation out of transportation policy and out of the Canada Transportation Act and into the hands of those departments which do have responsibility for regional development: Industry Canada through its economic development programs, Human Resource Development, through its training programs, and Agriculture Canada through its initiative, Canadian Rural Partnerships, among others.

There are a number of advantages to an integrated approach, and admittedly, some concerns. One concern is that by removing that “declaration”, and any vestige of an onus on the part of Transport Canada to deliver extraordinary transportation services, the government would be “let off the hook” too easily, and any hope of support would disappear.

I believe that this issue has been overstated. It should be a relatively easy step to include “transportation as an element of opportunity” as part of current development programs and include it in current funding if necessary. In fact, many development agencies are already being asked to support air transportation initiatives. By integrating air access within larger economic objectives, communities would create not only air, but multi-modal transportation access strategies that “link” to other elements of their programs: “helping build local solutions to local challenges”, in the words of the last Throne Speech.

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About the
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FAQCanada Site
Links and
Documents

Sections of the Speech

Introduction

Canada
and the World

Health Care in
the 21st Century

Children
and Families

Climate Change
and the
Environment

Talent and
Investment

Skills, Learning
and Research

Smart Regulation

Cities and
Communities

Government
and Citizens

Conclusion

The Canada We Want

SPEECH FROM THE THRONE

to Open the Second Session of the Thirty-Seventh Parliament of Canada

Honourable Members of the Senate, Members of the House of Commons, Ladies and Gentlemen:

It is a pleasure to greet you in the Jubilee Year of Her Majesty Queen Elizabeth II, whom we will be welcoming to Canada very shortly.

We also mark this year the 50th anniversary of Canadian Governors General. To celebrate this, we invited to Rideau Hall an energetic group of one hundred 17- and 18-year-olds from every province and territory to participate in a Youth Forum on creating community. In Gaspé, in Nunavut, on Haida Gwaii, all across the country, we are meeting young people who are becoming catalysts for change, as they take their place as leaders in the fields they choose.

It is exciting and encouraging to hear what young people are saying and what they are doing. Already, they are innovative. They are diverse. And they will change things. Some of them will do so through journalism, the arts, business or the labour movement. Others will devote themselves to civic and public life, perhaps becoming in time your successors, to carry on the democratic traditions of Parliament to which you are committing your lives. Nothing is more precious and valuable than our way of creating a society through the exercise of our democratic rights as citizens.

And the sacrifices that some of our citizens make are deeply appreciated by their country. My trip in April to Germany, where our fallen and injured were brought from the tragic incident in Afghanistan, was emotionally shared by all Canadians, many of whom have expressed how much the sacrifice of these men has meant to them.

This kind of contribution, this kind of democratic participation, this kind of nurturing of young leadership make us what we are as a nation. It is a very precious life that we share as Canadians. And we must be prepared not only to praise it, but also to make sacrifices for it.

Canadians today are confident about their personal prospects and Canada's future. Less than ten years ago, our economy was in decline, our deficit and debt were rising out of control, our unity was under threat, our confidence was shaken.

Today, because of our collective efforts, we have new opportunities, new possibilities and new choices for the Canada we want.

We have established the foundations for great success: fiscal sovereignty, a unified country and a confident people. We will not put at risk the accomplishments of the last decade. We will continue to be prudent and live within our means.

Maintaining our fiscal sovereignty and a dynamic economy allows us to reach higher. To find new solutions to enduring problems. To set new goals and ambitious targets. To take responsibility for building the Canada we want, for ourselves and for future generations.

We now have a generation of Canadians who have grown up in the Internet world, a generation of Canadians who are global, at ease with change and diversity, optimistic and eager to create, innovate and excel. And who believe they can achieve their aspirations in Canada. Canada must tap into and unleash this energy.

The goal of the government is nothing less than making Canada a land of ever-widening opportunity. Ensuring that the benefits of the new economy touch every community and lift every family and every Canadian.

Working together, we can put in place the health care system for the 21st century. We can get Canada's children off welfare. We can close the gap in life chances between Aboriginal and non-Aboriginal Canadians. We can tackle the challenge of climate change. We can be a world leader in innovation and learning, a magnet for talent and investment. We can build world-class cities and healthy communities. We can strengthen the bonds of shared citizenship and the partnership between government and Canadians. We can secure our place in North America and in the world as a mature country, confident in who we are and where we are headed.

This is the time for Canada.

✦ Canada and the World

We live in uncertain times. The events of September 11 demonstrated that our progress at home can be affected in a moment by world events. We see unrest in many parts of the world. We still see far too much poverty.

The government will continue to work with its allies to ensure the safety and security of Canadians. Canada will continue to work through organizations such as the United Nations to ensure that the rule of international law is respected and enforced. At the same time, the government will remain vigilant and ready to ensure the protection of Canadians from emerging threats, and will work with the United States to address our shared security needs.

But there is more we can do. Canada has a long history of contributing solutions to global problems. We will continue to speak out in every forum for the values of pluralism, freedom and democracy, and contribute to reducing the growing global divide between rich and poor. We will double our development assistance by the year 2010, and earmark at least half of that increase for Africa as part of Canada's support for the New Partnership for Africa's Development. As of January 1, 2003, Canada will eliminate tariffs and quotas on almost all products from the least-developed countries.

In the face of rapid change and uncertainty, the government must engage Canadians in a discussion about the role that Canada will play in the world. Before the end of this mandate, the government will set out a long-term direction on international and defence policy that reflects our values and interests and ensures that Canada's military is equipped to fulfill the demands placed upon it.

✦ **Putting in Place the Health Care System for the 21st Century**

No issue touches Canadians more deeply than health care. Our health care system is a practical expression of the values that define us as a country. Of the willingness of Canadians to share risk and accept responsibility for one another.

In 2000, all First Ministers reached an agreement on health care that reinforced our collective commitment to the principles of medicare, to working collaboratively to reform our system and to measure and report on our progress. Resources were provided. Work is proceeding. And the first public report is now available.

Building on this work, Roy Romanow was appointed to lead a commission on the longer-term future of Canada's publicly funded health care system. He will report in November.

The Prime Minister will convene a First Ministers Meeting early in 2003 to put in place a comprehensive plan for reform, including enhanced accountability to Canadians and the necessary federal long-term investments, which will be included in the next budget.

At the same time, the government will move ahead with an action plan in health policy areas under its direct responsibility. Under this plan, it will renew federal health protection legislation to better address emerging risks, adapt to modern technology and emphasize prevention. The government will take steps to strengthen the security of Canada's food system and reintroduce pesticides legislation to protect the health of Canadians, particularly children. It will work with its partners to develop a national strategy for healthy living, physical activity and sport, and will convene the first ever national summit on these issues in 2003. The government will take further action to close the gap in health status between Aboriginal and non-Aboriginal Canadians by putting in place a First Nations Health Promotion and Disease Prevention strategy with a targeted immunization program, and by working with its partners to improve health care delivery on-reserve.

The government will also modify existing programs to ensure that Canadians can provide compassionate care for a gravely ill or dying child, parent or spouse without putting their jobs or incomes at risk.

✦ **Helping Children and Families Out of Poverty**

Five years ago, Canada's governments launched the National Children's Agenda, engaging Canadians in every part of the country on how to ensure that all Canadian children have a good start in life; that families with children have the tools they need to provide care and nurturing.

No investments have greater payoff. No investments do more to break the cycle of poverty and dependency, and to maximize the potential of every Canadian.

The government will put in place a long-term investment plan to allow poor families to break out of the welfare trap so that children born into poverty do not carry the consequences of that poverty throughout their lives. It will again significantly increase the National Child Benefit for poor families, and will work with its partners to increase access to early learning opportunities and to quality child care, particularly for poor and lone-parent families. It will

also put in place targeted measures for low-income families caring for severely disabled children, to help meet the needs of the child and of the family.

The government will take additional measures to address the gap in life chances between Aboriginal and non-Aboriginal children. It will put in place early childhood development programs for First Nations, expanding Aboriginal Headstart, improving parental supports and providing Aboriginal communities with the tools to address fetal alcohol syndrome and its effects. The most enduring contribution Canada can make to First Nations is to raise the standard of education on-reserve. The government will work with the recently created National Working Group on Education to improve educational outcomes for First Nations children, and take immediate steps to help First Nations children with special learning needs.

Parents have the primary responsibility for providing their children with the tools to learn and develop. But Canadians also have a collective responsibility to protect Canada's children from exploitation in all its forms, and from the consequences of family breakdown.

The government will therefore reform the Criminal Code to increase the penalties for abuse and neglect, and provide more sensitive treatment for children who take part in justice proceedings as victims or as witnesses. It will also reform family law, putting greater emphasis on the best interests of the child; expand the Unified Family Courts; and ensure that appropriate child and family services are available.

◆ The Challenge of Climate Change and the Environment

Canadians know that our health and the health of our children, the quality of life in our communities and our continued economic prosperity depend on a healthy environment.

On a global scale, the problem of climate change is creating new health and environmental risks and threatens to become the defining challenge for generations to come.

As a northern country, Canadians will feel some of the effects of climate change sooner than will others. As a prosperous country, we must and will do our part.

As part of the Kyoto Protocol, Canada agreed to obligations to reduce greenhouse gas emissions by 2012. Extensive consultations and preparatory work followed. The government is now intensifying consultations with Canadians, industry and provinces to develop an implementation strategy to meet Canada's obligations over the next ten years. Before the end of this year, the government will bring forward a resolution to Parliament on the issue of ratifying the Kyoto Protocol on Climate Change. Meeting this challenge must become a national project, calling upon the efforts and contributions of all Canadians, in all regions and sectors of the economy — producers and consumers, governments and citizens.

To conserve our wilderness areas, clean water sources and key habitat, the government will create ten new national parks and five new National Marine Conservation Areas over the next five years. It will improve the ecological integrity in Canada's existing national parks. It will reintroduce legislation to protect species at risk.

The government will accelerate the clean-up of federal contaminated sites

in Canada. It will work with the United States to further improve air quality. It will accelerate its work with the provinces on improved national water quality guidelines, and ensure their implementation in areas of federal jurisdiction.

◆ A Magnet for Talent and Investment

The Canada we want requires a strong economy. The government will maintain its unwavering commitment to balanced budgets, disciplined spending, a declining ratio of debt-to-GDP, and fair and competitive taxes. It will build on its investments in research, literacy and education, and in competitive cities and healthy communities. It will also adjust its policies to enhance the climate for investment and talent. The government will reallocate resources to the highest priorities and transform old spending to new purposes.

● Skills, Learning and Research

The fuel of the new economy is knowledge. The government has invested heavily in providing Canada's schools and libraries with the information technology to connect young Canadians with the best information and knowledge the world has to offer. It has invested in access to universities and in excellence in university research because Canada's youth need and deserve the best education possible, and Canada needs universities that produce the best knowledge and the best graduates.

The government will build on these investments. It will continue to increase its funding to the federal granting councils to provide young Canadians greater support for graduate studies and research. It will work with universities on the indirect costs of research and on strategies for its commercialization to create opportunities for entrepreneurs and to fuel innovation. It will continue to work with small- and medium-sized enterprises in the development and application of new technologies in traditional and emerging sectors.

It will strengthen government science, integrating its efforts across departments and disciplines, and focussing on the priorities of Canadians.

In November, the Government of Canada will host the National Summit on Innovation and Learning. This will be an opportunity to position Canada as a world leader in such areas as health sciences, biotechnology and clean energy.

The economy of the 21st century will need workers who are lifelong learners, who can respond and adapt to change. Canada's labour market programs must be transformed to meet this challenge. To this end, the government will work with Canadians, provinces, sector councils, labour organizations and learning institutions to create the skills and learning architecture that Canada needs, and to promote workplace learning. This will include building our knowledge and reporting to Canadians about what is working and what is not.

The Youth Employment Strategy has been successful in increasing job opportunities and experience for young Canadians. But the employment needs of our youth are changing. Government strategies have to keep pace. Working with youth and other partners, the government will redirect its resources in this area to develop

skills for the future and to help those who face the greatest barriers to employment. It will also work with the provinces to fast-track a comprehensive agreement to remove barriers to participation in work and learning for persons with disabilities.

The government will promote entrepreneurial skills and job creation among Aboriginal people by increasing support for Aboriginal Business Canada. It will also tailor and target its training programs to help Aboriginal and Inuit people participate in economic such as the development of Voisey Bay, northern gas pipelines and similar projects throughout Canada.

One of Canada's greatest assets — and a unique advantage in a globalized world — is our openness to immigrants from every corner of the globe. The demographic realities of an aging population and slowing labour force growth place an even greater premium on this immigration advantage. Canada must continue to be the country that immigrants choose to find hope, hospitality and opportunity.

The government will work with its partners to break down the barriers to the recognition of foreign credentials and will fast-track skilled workers entering Canada with jobs already waiting for them. It will also position Canada as a destination of choice for talented foreign students and skilled workers by more aggressively selecting and recruiting through universities and in key embassies abroad.

• Smart Regulation

The knowledge economy requires new approaches to how we regulate. We need regulation to achieve the public good, and we need to regulate in a way that enhances the climate for investment and trust in the markets. The government will move forward with a smart regulation strategy to accelerate reforms in key areas to promote health and sustainability, to contribute to innovation and economic growth, and to reduce the administrative burden on business.

As part of this strategy, the government will adapt its intellectual property framework to enable Canada to be a world leader on emerging issues such as new life forms. It will speed up the regulatory process for drug approvals to ensure that Canadians have faster access to the safe drugs they need, creating a better climate for research in pharmaceuticals. It will work with provinces to implement a national system for the governance of research involving humans, including national research ethics and standards.

The government will revise Canadian copyright rules to ensure that Canada has a progressive regime that supports increased investment in knowledge and cultural works.

It will reintroduce legislation to amend the Canadian Environmental Assessment Act. It will also streamline environmental assessment processes, including implementing a single window for projects such as the northern pipeline. To pursue its strategy over the longer-term, the government will create an External Advisory Committee on Smart Regulation to recommend areas where government needs to redesign its regulatory approach to create and maintain a Canadian advantage.

The government will implement the recently announced Agricultural

Policy Framework and related measures to promote innovation in that key sector, which is vital to rural Canada and all Canadians.

The Canada-US Smart Border Declaration contributes to both our national security and the free flow of people, goods and commerce across our shared border. The government will build on this work and increase its consular presence to expand fair and secure trade and commerce, and to brand Canada in the United States. It will continue to work bilaterally and multilaterally to resolve trade disputes over softwood lumber and agriculture.

Recent events in the United States have weakened confidence in capital markets, not only in that country, but around the world. The government has been working closely with all parties to bolster investor confidence and improve the efficiency and integrity of Canadian capital markets. In this regard, it will review and, where necessary, change its laws and strengthen enforcement to ensure that governance standards for federally incorporated companies and financial institutions remain of the highest order.

Many investors and businesses have expressed concern that Canada's fragmented securities regulatory structure is inadequate and an obstacle to growth. They have urged reform to ensure that businesses can efficiently access the financing they need to grow, and to assure Canadians that they will be treated fairly when they invest. Co-operation among governments will be necessary. The government will work with all participants to ensure that Canada has the modern and efficient securities regulatory system it needs.

• **Competitive Cities and Healthy Communities**

Competitive cities and healthy communities are vital to our individual and national well-being, and to Canada's ability to attract and retain talent and investment. They require not only strong industries, but also safe neighbourhoods; not only a dynamic labour force, but access to a rich and diverse cultural life. They require new partnerships, a new urban strategy, a new approach to healthy communities for the 21st century.

Modern infrastructure is key to the prosperity of our cities and the health of our communities. Working with provinces and municipalities, the government will put in place a ten-year program for infrastructure to accommodate long-term strategic initiatives essential to competitiveness and sustainable growth. Within this framework, it will introduce a new strategy for a safe, efficient and environmentally responsible transportation system that will help reduce congestion in our cities and bottlenecks in our trade corridors.

It will extend its investments in affordable housing for those whose needs are greatest, particularly in those Canadian cities where the problem is most acute. It will extend the Supporting Communities Partnership Initiative to provide communities with the tools to plan and implement local strategies to help reduce homelessness.

In a number of cities, poverty is disproportionately concentrated among Aboriginal people. The government will work with interested provinces to expand on existing pilot programs to meet the needs of Aboriginal people living in cities.

The government will target its regional development activities to better meet the needs of the knowledge economy and address the distinct challenges of Canada's urban, rural and northern

communities.

The government will work with Canada's largest cities to develop targeted strategies to reduce the barriers faced by new immigrants in settling into the social and economic life of their new communities. It will introduce targeted measures to help children of recent immigrants to learn French and English, so that they can realize the opportunities that brought their parents to this country.

The government will also implement a national drug strategy to address addiction while promoting public safety. It will expand the number of drug treatment courts. It will act on the results of parliamentary consultations with Canadians on options for change in our drug laws, including the possibility of the decriminalization of marijuana possession.

◆ A New Partnership Between Government and Citizens

Canada has a unique model of citizenship, based simultaneously on diversity and mutual responsibility. This model requires deliberate efforts to connect Canadians across their differences, to link them to their history and to enable their diverse voices to participate in choosing the Canada we want.

The government will ensure that as Canadians take charge of their future, they will have access to their history by creating a new institution that brings together the National Archives of Canada and the National Library of Canada, providing new tools to reach Canadians, young and old. It will also strengthen key arts and heritage institutions and protect significant historic sites and buildings.

It will create more opportunities for young Canadians to help clean up our environment and assist in achieving Canada's global priorities, particularly in Africa.

It will reform our citizenship legislation to reassert the rights and reinforce the responsibilities that go with being Canadian.

It will put into action the accord it signed with the voluntary sector last December, to enable the sector to contribute to national priorities and represent the views of those too often excluded.

The government will work with provinces toward renewal of legal aid so that Canadians can have access to adequate legal representation before the courts.

Linguistic duality is at the heart of our collective identity. The government will implement an action plan on official languages that will focus on minority-language and second-language education, including the goal of doubling within ten years the number of high school graduates with a working knowledge of both English and French. It will support the development of minority English- and French-speaking communities, and expand access to services in their language in areas such as health. It will enhance the use of our two official languages in the federal public service, both in the workplace and when communicating with Canadians.

The government will reintroduce legislation to strengthen First Nations governance institutions — to support democratic principles, transparency and public accountability, and provide the tools to improve the quality of public administration in First Nations communities. It will work with these

communities to build their capacity for economic and social development, and it will expand community-based justice approaches, particularly for youth living on reserves and Aboriginals in the North. The government will also work with Aboriginal people to preserve and enhance Aboriginal languages and cultures.

Canadians want their government to be open, accountable and responsive to their diverse and changing needs.

Early in this session, the government will provide clear guidance and better enforcement of the ethical standards expected of elected officials and senior public servants. The government will strengthen the legislation governing its relationship with lobbyists. And the government will introduce legislative changes to the financing of political parties and candidates for office.

Canadians know the value and importance of the role of government and of the need for excellence in the public service. The government will introduce long-awaited reforms for the public service to ensure that it can attract the diverse talent it needs to continue to serve Canadians well.

✦ Conclusion

The Canada we want cannot happen by government acting alone or by citizens acting apart.

We know that by pursuing the common good, we pursue our own good; a country is more than a collection of narrow interests, it is a common enterprise to which all can contribute.

The priorities we have outlined today build on the conviction that we must add to the work of our ancestors, and leave Canada a better place for future generations.

May our future, like our past, be a story of achievement.

Fellow Canadians:

Respectful of our history, confident in our future, let each of us do our part.

Members of the House of Commons:

You will be asked to appropriate the funds required to carry out the services and expenditures authorized by Parliament.

Honourable Members of the Senate and Members of the House of Commons:

As you carry out your duties and exercise your responsibilities, may you be guided by Divine Providence.

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[Important Notices](#)

There is controversy around some of the regional development programs and agencies. Some see them as costly, ineffective and having perverse impact on the development of a sustainable local economy. While these arguments may have some merit, the fact is these programs exist to help equalize opportunities for growth across the country. It seems more reasonable to include air access as an element in these programs, and work to improve their success rate, than to “throw the baby out with the bathwater”.

A significant advantage of including air access as a part of economic development is that it opens the table to a broader constituency and possibly, more funding mechanisms. For example rather than rely just on Transport Canada, communities could work with a number of agencies and government departments from both federal and provincial/territorial levels of government which then could work together to provide resources that meet the unique needs of each community.

Developing Regional Air Services

If one of Canada’s air policy goals is to create competition, then one cannot look at regional access issues without looking at the challenges faced by independent regional carriers. These carriers provide the essentials of life to remote communities. They are often locally owned, and operators live in the communities they serve. They are invaluable and unique links in the transportation system, and their continuation and growth may be essential to thousands of Canadians.

However, they face a number of barriers. One significant obstacle is the dominance of Air Canada and the impact of that dominance on third-tier carriage in Canada. Regional carriers that have an alliance with Air Canada, have significant advantages over those that do not. In a way, they are part of the Air Canada “family” and offer the benefits of fully networked air service. They get favourable “pro-rates” on connecting flights. Depending on the type of partnership, they often may offer not only standard Aeroplan points, but the desirable “Status” miles as well. Independent carriers have virtually none of these advantages.

It is also difficult for third-tier carriers to feed directly into international carriers at the international gateway hubs, although in theory, they are able to do so. It is one thing to be able to feed into Air Canada or Jazz and from there into Star Alliance. It is quite different when a carrier with minimal service tries to feed into an international network.

A companion issue is a lack of investment. Investment in the airline sector is problematic at the best of times, but third-tier carriers that are “flying solo”, either in competition with Air Canada or its partners, or without inclusion in the Air Canada network and access to AC’s resources, face an even more difficult challenge.

A new challenge to third-tier is the entrance of low-fare jet service to medium or even small communities, which not only stimulates demand, but also draws existing de-

mand from wide catchment area. So, independent third-tier carriers are faced with a double whammy: competing against networked carriers or low-fare jet service. All of this on thin routes, where there are not large numbers of passengers.

In one sense, the current state is simply the marketplace at work, and third-tier independent carriage may always be minimal. However, given the importance of the service they can provide to smaller communities, the problem cannot simply be ignored.

The Government of Canada recognized that these issues are serious and introduced a number of provisions in Bill C-26 and in the undertakings with Air Canada to mitigate them to a degree. Recommendations on further action that may be required regarding Bill C-26 are reviewed in the next section of this report. However, given the lack of sustained development of regional service over the last four years, these provisos may not be sufficient. I believe that it is time for new thinking around "third-tier" carriage and what it means for the development of competitive or new services.

Essential Air Services Program

Another option to deal with regional air access is to introduce a Canadian version of the U.S. "Rural Air Services Survival Act" also known as the "Essential Air Services Program", administered by the U.S. Department of Transportation. This government-funded program provides limited service (typically 19-seaters) from communities that are at least 70 miles (110 kilometre) away from another airport that have lost their scheduled air service to a hub. The program in the U.S. has an annual budget of \$50 million.

The advantage of applying a version of this program in Canada is that it can be kept quite small, and as long as the "firewalls" around admissibility are strong, reasonably easy to contain. It could support smaller regional carriers, if that provision is included as one of its criteria. It can link small communities into the national air system. However, while a program like this has some benefits, it also raises some thorny challenges.

The U.S. program began as a "temporary" transition program in the U.S. when the airline industry was deregulated in 1978. In 2002, it is not only still going strong, but has been expanded. Even then, it is not sufficient for some. Critics of the Rural Air Services Survival Act claim that it does not go far enough to provide sustainable service – raising the spectre of endless, ever-increasing costs to taxpayers.

Another issue, as noted in a previous section is that this purely "transportation" solution only partially addresses the complex relationship and the impact air access has on local economies. The problems of rural communities (dwindling and aging populations, the challenge of economic diversification) will not be solved simply because people can fly to a hub.

The possible exception is for those communities for which air access is truly “essential”, i.e. when the community relies mostly or solely on air access as its primary means of transportation. Currently, northern Canadian communities tend to have good scheduled service, without subsidizing air carriers.

As well, there are other forms of assistance. Transport Canada provides some funds through the Airport Capital Assistance Program that supports eligible applicants in financing capital projects related to safety, asset protection and operating cost reduction. Transport Canada also financially supports or operates 13 remote airports that provide the only reliable means of year-round transport to isolated communities.

Take No Action

The government could choose to do nothing, and let the marketplace unfold. This solution has some appeal, especially to those who promote market-based solutions. There would be no distortion of the market. There would be no possibility of government picking “winners and losers”. Communities that want better air access would be encouraged to develop a strong knowledge base, work with the carriers, and design their own resolution.

While this may be the “purest” solution, it would be unpalatable to many who see Canada’s commitment to help disadvantaged communities as a key element of public policy.

5.0 Government Policy Recommendations: Air Access and Economic Development

Development

- 5.1 That, to more effectively serve the needs of community development, the Government of Canada separate economic development policy from transportation policy, by removing the declaration in Section 5 of the Canada Transportation Act of 1996.**
- 5.2 That, when market forces are not sufficient, the Government of Canada expand the use of existing economic development tools and funding mechanisms to enshrine air access as part of these programs, and as a integrated element in community planning that contributes in a measurable way to overall development strategies.**

- 5.3 That departments in the Government of Canada that have an interest in community access issues (e.g. Transport Canada, Industry Canada, Agriculture Canada, Human Resource Development etc.) work together, as well as with their provincial and territorial counterparts, to create common air access strategies based on local needs.**

Regional Service

- 5.4 That the Government of Canada review all aspects of current transportation and taxation policies' impact on air service to smaller communities and on third-tier carriers, to ensure that the policies create an environment that encourages the growth and viability of these carriers. Changes or additions to policy should be made if it is found to be counter-productive to the development of third-tier carriage to small communities**
- 5.5 That the Government of Canada consider the option of a "small carrier" strategy that would encourage the growth of regional service.**

Other governments and other departments

Over and above the government departments that are concerned with economic development, there are a number of government bodies that are either affected by the availability or quality of air service, or influence it through their own programs. One example is provincial and territorial governments. They have no direct responsibilities for air service, but are very much affected by the level of service their communities receive. Their interest extends beyond their departments of Transportation, and includes Municipal Affairs, Industry and Economic Development, among others.

Federally, departments whose policy affects the airline industry include the departments of Finance, Industry, Foreign Affairs and International Trade, Immigration, Customs and Indian and Northern Affairs.

The departments and governments should meet on a regular basis to review the state of the airline industry, and the effect of their combined policy actions on it. For example, Finance was responsible for the imposition of the Air Travellers Security Charge and is only now beginning to look at the impact its decision has had on people who fly.

6.0 Government Policy Recommendations on including other departments and other levels of government:

- 6.1 That the Government of Canada take the lead to establish new communications mechanisms between levels of government and other federal government departments which are either impacted by or impact the quality and type of air service Canadians receive.**

Meaningful Data

The Airline Observer's Third Interim Report²⁴ dealt in detail with the issues around data collection and dissemination. In brief, little public data is available to stakeholders such as communities or airports who could use the information to attract new carriers, market their communities or undertake a rigorous analysis of their air access needs. Some data are available for purchase, such as the Official Airline Guide. However, these types of information sources tend to favour those who have a degree of sophistication to interpret the data, and/or the finances to hire experts. The usual public avenue of release of detailed data by Statistic Canada is not possible given Air Canada's dominance, as to do so would contravene commercial confidentiality requirements in the Statistics Canada Act.

With the obvious exception of carriers, the call for more detailed timely data is fairly widespread and consistent. The Canada Transportation Act Review Panel stated:

"Better data would facilitate more in-depth research, would give observers a better basis for assessing the performance of Canadian carriers and would help participants and potential entrants identify new opportunities...the government and transportation industries expand the collection of transportation data and develop new procedures to reflect changes occurring in the domestic and global economies."²⁵

It is also worth noting that very detailed data are collected and disseminated in the United States.

Transport Canada has recognized that there are gaps in the data currently available both to government and the public, and has taken two important steps. The first was the presentation of a one-day Aviation Forum, at which all stakeholder groups, including airlines, could share their views and concerns. One of the outcomes of the Forum was the creation of a "data gaps" analysis that has given stakeholders a clearer idea of what is and is not currently available. The second was the implementation of a pilot project that uses an automated system to collect and analyse data, thereby eliminating an unnecessary paper burden on airlines. The Minister and government are to be commended for their actions in both these areas.

²⁴ *Airline Restructuring In Canada, Third Interim Report*, Debra Ward April 2002

²⁵ *Vision and Balance*, Report of the Canada Transportation Act Review Panel, June 2001

Electronic collection holds promise to solve the paper burden problem. The most difficult problem remains, though: disseminating data to stakeholders in a way that balances the benefits of increased information with the needs of carriers to protect sensitive information.

The government must weigh the incumbent carriers' needs with those of the other interested stakeholders: communities, airports, competing carriers and potential investors. If regional service is to be improved, if competition is to grow, if we are to better understand the complex relationship between air service and the economy, we must have timely and reasonably detailed information. If consumers are to understand problems that arise because of circumstances, such as bad weather, or because of carriers' inefficiencies, they too must have consistent and comparable information.

Government is also a stakeholder in data needs. For example, the U.S. government uses its data to assist in transportation decision and policy making; to negotiate international agreements; to monitor competitive behaviour; to analyze anti-trust and merger activities; to assist in planning airport and airways, as well as other uses. It is reasonable to think that the Government of Canada would benefit from similar knowledge. Simply requiring that the data be collected and be accessible to appropriate government departments and officials can solve this issue. Since this data would not be made public, it would not threaten carriers' competitive positions.

Publicly available data which guarantees full confidentiality is probably never possible. Even in the United States, hubs are dominated by as much as 80% by only one carrier. Data on origin/destination, loads and average fares, as well as consumer-related data is made public even when the data can be clearly related to one carrier. Release of these data helps not only stakeholders but carriers as well, according to the U.S. Department of Transportation, which stated:

"A few carriers, initially reluctant to collect and report the required statistics, later recognized the benefits of the structure and content of the information"²⁶

Alternatively, we could wait until conditions are "fairer". More competitors on more routes would mean that it would be difficult to pick out the information on any single carrier, which would make release by Statistics Canada possible. However, that's a bit of a vicious circle, as competition may be restricted precisely because there is little data.

Rather than wait indefinitely, a new process for public dissemination should begin now. Several steps must be taken to allow access to reasonable data by non-government stakeholders. The first is to ensure the right data is collected in a timely and useful manner. The second is to determine what information is really required by stakeholder groups to create a competitive environment, to assess quality of service

²⁶ U.S. Department of Transportation, Bureau of Transportation Statistics, "Collection and Distribution of Airline Statistical Information at the United States"

and to achieve other goals. The third is to create a data strategy and tools that provide useful information for stakeholders, and try to ensure that carriers' interests are respected. However, carrier confidentiality of data must be weighed against the larger "community of interest".

7.0 Government Policy Recommendations: Data

- 7.1 That the Government of Canada pursue a policy of more open and accessible aviation data, building on its work of the Aviation Forum on Data, the subsequent "data gaps" analysis and the technologically-based pilot project.**
- 7.2 That the Government of Canada enact appropriate legislation to collect detailed data on airline operations, particularly those data needed for government policy and oversight.**
- 7.3 That the Government of Canada continue to work with stakeholder groups to develop a data strategy that clearly determines which data should be disseminated publicly, in what form and to serve what purposes.**
- 7.4 That the Government of Canada accept that while the confidentiality of carriers' data should be respected whenever possible, the needs of this constituency must be balanced with the needs of the larger "community of interest" and with the potential benefits to the Canadian economy and communities.**

What Should Government Be Doing About the Airline Industry in the Short-term?

Bill C-26

Bill C-26 re-imposed a form of regulation on the airline industry, particularly Air Canada. It was seen as a temporary measure, created to ensure “an ordered restructuring of Canada’s airline industry, with the least possible disruption to communities, the travelling public and to airline employees”, based on five principles:

- Protection from price gouging
- Protection of service to small communities
- Fair treatment of employees
- Fostering of competition
- Maintenance of Canadian ownership and control

The provisions of Bill C-26 and the Air Canada undertakings are best seen as government-created substitute for a competitive market. Theoretically, as restructuring ends and competition grows, the need for some of these measures will disappear. In fact, all of the undertakings with Air Canada have time limits ranging from two to seven years and those that still are in effect are subject to review.

Questions to be asked about Bill C-26 and the undertakings are:

- Are these provisions, created in 1999 and 2000, still relevant post-September 11th?
- Have competitive market forces begun to mitigate the dominance of Air Canada?
- Have the measures served their purpose?
- Should any be extended past their current time frame?
- Should any be reduced (or increased) in power?
- Are the measures being implemented effectively?
- Are there any other changes that should be made?

When reviewed in detail, the provisions are surgical and specific. The government has walked a fine line between leaving too big a footprint and distorting the market, and still being able to take action when needed. While arguably, they may have fallen off the high wire on occasion, this balanced approach, while difficult to achieve, is sound.

This does not answer the concerns of people who feel that the airline system is not working, and that regulations that are more stringent are needed. Bill C-26 has not re-regulated the airline industry, but has simply attempted to mitigate the more perverse effects of dominance and monopoly. The government cannot “step in” in

any large way. However, unless otherwise noted for specific provisions listed below, in general, I believe that the government's level of protection is acceptable, and further powers to regulate aspects of the marketplace are not warranted at this time.

Protection from Price Gouging

This provision gives the Canadian Transportation Agency (CTA) the ability to disallow, roll back or refund any "unreasonable" fares on monopoly routes. The Agency can act on a complaint or, for a limited period, on its "own motion": in other words, institute its own investigations. However, this provision does not extend to competitive routes.

Some organizations, such as the Public Interest Advocacy Center, believe this measure does not go far enough, and should be expanded to include the authority to review the actual cost of all air fares in Canada and to approve or change prices for different classes of tickets. Unsurprisingly, Air Canada has suggested that the measure goes too far, and impedes the carrier's ability to set prices. The Canada Transportation Act Review Panel suggested that the process was too complex and that the provision should be eliminated.²⁷

Objectively, there has been relatively little public outcry: about two per cent of all complaints and three per cent of complaints against Air Canada received by the Air Travel Complaints Commissioner were about fares²⁸.

A real issue, and one that affects the efficacy of government action, is that governments tend to be cautious and deliberate, which translates to slow – too slow, in some cases, to react in a timely way to rapid changes in the market. The CTA is trying to overcome this challenge by building a template: a body of information and knowledge that will allow it to move more quickly and efficiently. However, this speed will be relative. The Agency might be able to move more quickly, but not as quickly as the market itself. This is a limitation of any government intervention, and one of the reasons why a competitive and self-correcting market provides quicker and more effective answers.

Weighing the pros and cons, there are a number of reasons to continue this provision, as is, the chief one being that there are 152 communities that are served by only one carrier. In my view, the measure to protect Canadians from price gouging on monopoly routes strikes a reasonable balance between a free market and consumer protection and should be continued. To ensure fairness, I urge the CTA to move rapidly to address issues related to their ability to render judgements that are both timely and accurate.

²⁷ *Vision and Balance*, Report of the Canada Transportation Act Review Panel, June 2001

²⁸ Air Travel Complaints Commissioner Third Report, April 2002

8.0 Recommendation on Protection from Price Gouging:

- 8.1 That this provision continues without change, but that the Government of Canada take measures to ensure timely and accurate judgements, and that success in this regard is monitored on an ongoing basis.**

Protection of Service to Small Communities

Two provisions protect small communities. The first was an Air Canada obligation to serve all communities that were being served in December 1999 by Air Canada, Canadian Airlines Corp. or their wholly owned subsidiaries. This commitment is in effect until the end of this year. The second provision requires air carriers to give 120 days notice before discontinuing year-round, non-stop scheduled air services between two points in Canada where the proposed discontinuance of service will result in a significant reduction of weekly passenger-carrying capacity between those two points. As well, the carrier has to provide an opportunity for elected officials of the municipal or local government to meet and discuss the impact of the proposed discontinuance or reduction.

The first provision is intended to give time to communities to lessen their reliance on Air Canada, and look for locally based solutions. Community officials with whom I have spoken over the last two years have become far more realistic and more sophisticated in dealing with the issues, and with airlines. I also believe that there are a number of smaller carriers across the country that would step in, very effectively, if Air Canada were no longer serving a community. This would have the benefit of helping develop more independent carriage in Canada.

The second provision applies to all carriers. Formerly, carriers were able to exit a community with 60 days notice, and did not have to contact local elected officials. This new approach is intended to give communities more time to plan and an ability to discuss the carrier's decision and explore new options.

The usefulness of the new provisions around exits will best be judged more fully once Air Canada can exit communities. It is almost impossible to judge the efficacy of this measure until then, and I therefore recommend that no changes be made at this time, but that the provision be monitored closely over the next year or two.

9.0 Recommendation on Protection of Service to Small Communities:

9.1 That the 120-day exit provision continue without change, but that the Government of Canada monitor its efficacy in the following areas:

- **Outcomes of airlines' discussions with elected officials**
- **Measurement of the appropriateness of the 120-day provision to ensure that it provides enough time for community action, but does not deter new entrants**

Consumer Protection

There are two provisions in Bill C-26 designed to assist consumers. These are the Air Travel Complaints Commissioner's position as a temporary member of the Canadian Transportation Agency, and the extension of the Agency's jurisdiction over both domestic and international tariff complaints.

Additionally, as part of my mandate, I have also investigated the need for a "Passengers Bill of Rights".

Air Travel Complaints Commissioner

The Air Travellers Complaints Commissioner plunged into a maelstrom of anger at his appointment in summer 2000. People's complaints against airlines, especially Air Canada, were numerous and furious. Flights were oversold and people were bumped. Flights were cancelled without notice. People were left in limbo on the phone, sometimes for hours. Even frequent flyers felt they were getting short shrift while they still paid top dollar. "Air rage" was front page news.

Since then, Air Canada has put its own Ombudsman in place, and enhanced its quality and service commitments to passengers through its voluntary Customer Service Plan. Complaints to the Commissioner have declined a bit. There are still problems, but they have abated. I believe that some of this progress is a direct result of the creation of the Complaints Commissioner position, and the effectiveness of Bruce Hood, the first Air Travel Complaints Commissioner.

This position, originally intended to provide an avenue of redress where a person is not satisfied with the response of an airline to a complaint, has also provided an important and successful method to measure consumer reaction to changes in the airline sector through the Commissioner's semi-annual reports. It has also provided the CTA with an informal process to redress complaints, an important addition to its arsenal, which in other areas is highly structured and formal. As well, there are indications that Air Canada has improved its own customer relations significantly, and may be resolving most of the complaints on its own, without the need for pas-

sengers to take it to the next stage of registering a complaint with the Air Travel Complaints Commissioner.

The Commissioner has no regulatory power, and uses informal mediation and “moral suasion” to resolve issues. While some people have called for an extension of these powers, I believe this is not required at this time. An informal process allows issues to be resolved relatively simply and quickly. If a legal or regulatory framework were to be imposed, the Complaints Commissioner, and complainants would be subject to the same deliberate and slow “due process” that affects the Agency’s ability to render judgement in a timely manner.

While I do not see the need to provide the Commissioner with additional powers at this time, the position and its outcomes should be monitored by the government to ensure that complaints are handled quickly and efficiently, and that consumers are satisfied that the process is working. If it can be demonstrated that further powers are required, action can be taken later.

10.0 Recommendation on the Air Travel Complaints Commissioner:

10.1 That the Government of Canada continue the role of the Air Travel Complaints Commissioner, and that the Commissioner’s work be monitored to ensure that complaints are handled in a timely and effective manner and that the Commissioner has all necessary powers.

Tariffs

The air carrier’s tariff contains all its fares, rates, charges, and terms and conditions of carriage. A ticket is proof of payment and only contains some of the information that appears in a tariff. The tariffs cover a number of things such as: limits or restrictions on the weight or size of baggage, compensation for lost, delayed or damaged luggage, compensation for denied boarding (bumping), and the carrier’s rules concerning the carriage of persons with disabilities. The tariffs must be published by law, but in practical terms, they are long and complex and not readily accessed by the public. Not many passengers know all the terms and conditions of their contract with carriers.

The CTA has a number of powers over tariffs. It may:

- Fine a carrier if it has not applied the terms and conditions of its tariff
- Order a carrier to apply its terms and conditions of carriage if it has failed to do so

- Under certain circumstances, order carriers to compensate passengers or shippers if the tariff was not applied
- Disallow a tariff term or condition if it is found unreasonable or unduly discriminatory, and may substitute a different term or condition in its place

These provisions are helpful, but the CTA's ability to ensure "reasonableness" for consumers is hampered by the lack of public awareness about the tariffs and what they contain.

The two issues go hand-in-glove: it is difficult to mount a successful complaint if you do not know what the rules are. This lack of information is a barrier to consumer action.

Presenting and communicating tariffs to the public is a complex and difficult process. Nonetheless, I believe it is a necessary step. The ability of the CTA to act on behalf of wronged consumers is only as great as consumers' ability to understand the conditions of contract. An additional recommendation for action, which requires the cooperation of carriers, will be found in the section, Issues and Recommendations for Stakeholders.

11.0 Recommendation on Tariffs:

- 11.1 That the Government of Canada ensure that the complaint process relating to tariffs is easily accessed by consumers and is "user-friendly".**

Do We Need A Passenger Bill of Rights?

No. There are a number of reasons why this approach to consumer issues is not only overkill, but would be poor law. For one, Canadians are currently protected by a number of different consumer laws under provincial jurisdictions. There are additional provisions to protect consumers under the Competition Act (misleading advertising). As noted in the previous section, airline passengers can appeal to the Canadian Transportation Agency on tariff issues. We also have rights, and an avenue for recourse under the Official Languages Act when dealing with Air Canada. Finally, there is the court system. Ultimately, every consumer has the right to sue.

I also have to confess my personal distaste for the use of the profound and important concept of "rights" for something as prosaic as airline travel. There is a difference between having legal recourse if you do not get what you have paid for, and individuals' rights that are entrenched in the Charter of Rights and Freedoms. The right to free expression is a higher concept than the right to a perfume-free cabin. Rights belong to all of us, not only those of us who fly. This exposes a small companion issue: what about the "rights" of passengers of intercity buses or passenger rail?

The problem is not a lack of laws. The problem is a lack of knowledge. Following the disastrous summer of 2000 when the quality of air travel was abysmal, many carriers, including Air Canada, adopted voluntary Customer Service Plans that laid out their policies for lost baggage, bumping, and other unpleasant exigencies of the air travel “experience”. However, to find out what is in the Air Canada Plan, you have to get onto the carrier’s web site and do some digging and reading.

Similarly, unsatisfied passengers can challenge the tariffs, but they first have to know that 1) the tariffs exist and 2) what they contain. As discussed in the previous section, tariffs are difficult to find, and even more difficult to read. And as a last resort, if a passenger has exhausted all other means, s/he can sue. But where does one start? Most of us are not litigious, and have limited experience with the court system.

However, the mechanisms are there. The Small Claims Court of Ontario, for example, can render monetary penalties (including damages) of up to \$10,000, and the process is designed to be as simple and as speedy as possible. There is even a booklet on the Ontario government web site that tells people how to use the system²⁹. Other provinces have similar provisions.

All of these tools designed to protect consumers are only of marginal value if consumers are not aware of them. Airline passengers need to have easy access to all of this critical information, an objective that requires action by governments, the airline industry and perhaps other stakeholders.

There is another side to demands for “Passenger Bill of Rights”, which is a bit more vague, but has to do with “guaranteeing” quality of service. Understandably, people want to be assured that they won’t have to wait on the telephone for hours, deal with snippy staff or be treated rudely. While I sympathize, it must also be realized that there is no law that can protect consumers from an employee’s bad judgment, employers’ poor training or plain old stupidity. Realistically, the only real cure, and the only certain way to increase service standards, is by competition.

Harking back to my theme of “made for Canadians”, two obvious areas where Canadian companies’ service standards leapt by vast amounts when “foreigners” came into their markets are long distance telephone providers and high-volume, low cost retailers. There is a difference between the attitude of a company that is waiting for your dollar, and one which is fighting for it.

12.0 Recommendations on a “Passenger Bill of Rights”:

12.1 That the Government of Canada take no action to legislate a unique “Bill of Rights” for airline passengers, BUT

²⁹ *How to Make Small Claims Court Work for You*, Ontario Attorney General
<http://www.attorneygeneral.jus.gov.on.ca/html/cad/sccbbook.htm>

- 12.2 That the Government of Canada work with airlines, consumer groups and other levels and departments of government to provide “one-stop”, easily accessible information on what legal and regulatory tools are available to consumers.**

Fostering Competition

The requirement to foster competition takes up the bulk of the remaining provisions of Bill C-26 and the Air Canada undertakings. Most of these fall under the jurisdiction of the Competition Bureau, whose role is to promote and maintain fair competition so that Canadians can benefit from lower prices, product choice and quality services.

Special Provisions Under the Competition Act

The airline sector, and Air Canada are subject to special provisions under the Competition Act. This is an extraordinary circumstance as the Act is intended to provide laws of general application. The unique nature of the airline provisions has been an area of concern for some, notably the Standing Committee on Industry, Science and Technology that in a recent report stated:

“Today, Canadians are witnessing the enactment of “special rules for a special industry” — the air carrier services industry — into a framework law, as a result of the absence of a suitable deregulatory framework...At this time, the Committee acknowledges that the special provisions related to the airline industry are temporary measures that will be removed when healthy competition is realized within the industry. At the same time, the Committee is deeply concerned that this expectation will be long in coming, as even the United States (with about ten times the population of Canada) appears to be able to sustain only five or six nationally hubbed airline companies. Without the removal of the ownership and cabotage services restrictions, the industry may be destined to dominance by Air Canada for a protracted period. As such, the Committee is apprehensive about the government’s move from a law of general application to one that includes special provisions for a specific industry when other equally effective options may be available through forward-looking reform.”³⁰

These concerns are well founded, and the government should ensure that it moves away from “special provisions” as quickly as possible. Since, as the committee notes, “healthy competition” should replace these provisions, it would be appropriate for the government to take actions, as outlined elsewhere in this document, to encourage increased competitive air services in this country.

³⁰ *A Plan to Modernize Canada’s Competitive Regime*, House of Commons Standing Committee on Industry, Science and Technology, April 2002

13.0 Recommendation on Special Rules for the Airline Industry within the Competition Act:

- 13.1 That the government act on the concern expressed by the House of Commons Committee on Industry, Science and Technology and take action that will remove the special airline industry provisions from Competition law, and replace them with more appropriate and effective options as quickly as possible.**

Anti-predation measures

The Competition Bureau can take action against a dominant carrier that may be engaged in anti-competitive practices that entail running at a loss to kill the competition. Specific regulations respecting anti-competitive acts of persons operating a domestic service include³¹:

- Operating capacity on a route or routes at fares that do not cover the avoidable cost of providing the service, that is all costs that could be avoided if that service is not provided.
- Increasing capacity on a route or routes at fares that do not cover the avoidable cost of provided the service, that is all costs that could be avoided if the service is not provided
- Use of a low-cost second-brand carrier in a manner described in the two bullet points above

Under the recently passed Bill C-23, the government may also³²:

- Grant a further extension of the 80-day temporary “cease and desist” order until the Commissioner has had sufficient time to receive and review information required to determine whether to make an application before the Tribunal
- Impose an administrative monetary penalty of up to \$15 million against a dominant airline carrier which has been found to have abused its dominant market position
- Consider “aggravating or mitigating factors” including:
 - The frequency and duration of the practice in question

³¹ Bullet point information condensed from the Canada Gazette, 2000-08-30 Part II, Vol. 134. No. 18

³² Bullet point information condensed from “Amendments with Respect to the Airline Industry” backgrounder, Competition Bureau, 2002-06-21

- The vulnerability of the class of persons adversely affected by the practice
- Injury to competition in the relevant market
- The history of compliance with the Competition Act by the entity and;
- Any other relevant factor

These new powers seem to have been effective: both CanJet and Jetsgo entered the market following these changes, and CanJet cited the new laws to allow fair airline competition as one reason that it resumed service.

The grievance process begins with a complaint, which triggers an investigation by the Competition Bureau. If the Competition Commission finds evidence in support of the claim, he then takes the case to the Competition Tribunal, a separate quasi-judicial body. There are two current cases claiming that Air Canada engaged in anti-competitive practices. The Competition Tribunal has yet to render a judgement on either case brought by WestJet or CanJet, although the cases (or the complaints) are two years old or more. Part of the delay was attributed to September 11th and its aftermath. Still another was that these cases are the first of their kind. Not only are they setting precedent, but also there is a certain amount of delay as the proper systems are developed. Theoretically, once these rulings have been rendered, the Bureau and Tribunal processes will be smoother.

While the delay has been costly, it is possible that once these initial suits are determined, we will have a blueprint for the future, and the “rules of the game” will be much more simple and clear.

This provision is key to the growth of competition. The process, which is complex and protracted, must be reviewed carefully to be certain that this is the best way to determine and act on anti-competitive practices. The government must be prepared to make changes if it is not. After going through this intricate and difficult process, it is fair to wait a bit longer to assess the outcomes of the cases, but not much more beyond that point.

14.0 Recommendation on Anti-predation provisions:

- 14.1 That the Government of Canada closely monitor the cases before the Tribunal to ensure that the current criteria of “avoidable cost” and the Bureau’s new abilities under Bill C-23 are a fair, realistic and practical determination of anti-competitive behaviour in the airline sector, and to modify them, or take a new approach, if they are not.**

The Air Canada Undertakings

These are a series of temporary measures agreed to by Air Canada to mitigate its dominance. Some have already ended, such as the attempt to sell Canadian Regional Airlines, and the undertaking that Air Canada not start discount carrier operations in Eastern Canada for a specific period of time. This section examines some of the ongoing key undertakings and recommends further action where warranted.

Access to Aeroplan

Air Canada must sell its frequent flyer points to eligible Canadian carriers (with revenues of \$250 million or less) on commercially reasonable terms. In practice, this measure is not ideal.

- First, it promotes the use of a unique Air Canada product, Aeroplan, essentially extending AC's market reach, not containing it.
- Second, this undertaking applies only to the type of frequent flyer points that can be traded in for tickets on Air Canada flights. Air Canada (and its partners and subsidiaries) are the only carriers which offer "status miles": points which deliver frequent traveller perks of lounge access, priority lines and baggage claim, etc. In a competitive market, Air Canada retains a significant advantage by offering this unique product.
- Third, carriers have complained about delays in processing the paperwork and the need to submit to an Air Canada safety audit prior to getting access to the program.

This undertaking is to end in 2005. The ideal market solution would be the development of an alternative carrier network that fed into, and offered, competitive points (such as AAdvantage). However, without a more liberalized environment, this solution is unlikely to emerge in that short a period.

As a result, the next best solution is to ensure that the undertaking is as effective as possible, notwithstanding its limitations.

15.0 Recommendations on Aeroplan:

- 15.1 That the Government of Canada ensure, that in the absence of competitive frequent flyer plans, this program is readily and fairly accessible to independent carriers that wish to participate.
- 15.2 That in the continued absence of competitive frequent flyer plans, the commitment is extended past its current deadline, if necessary.

Interlining and Joint Fares

These undertakings ensure that Air Canada enters into interlining (e.g. baggage transfers, ticketing and bookings) and joint fare agreements with any Canadian carrier that so requests, subject to certain provisions (i.e. "meets reasonable industry standards").

This guarantees that any Canadian carrier can link into the Air Canada network, currently the only domestic network that serves both Canadian and international points.

This provides access, but not equality. An Air Canada "partner" third-tier airline could offer lower fares, better connections and even, at times, "status miles". These are significant competitive advantages over independent carriers and the advantages may be so powerful that they could stifle the development of competition on regional routes.

This problem is a direct outcome of the acquisition by Air Canada of Canadian Airlines Corp., each of which had its own regional and mainline network feeding into two different international alliances (Star Alliance for Air Canada and Oneworld for Canadian Airlines). The loss of CAC also meant the loss of Oneworld and all the opportunities for connectivity that it offered. Without a second network, it is difficult to imagine how third-tier regional carriage can develop much more than it has.

One possible solution is to make this provision tougher. For example Air Canada could be required to create equivalent "joint fares" for all third party carriers, whether they are partners or not, using a "most favoured nation" (MFN) system: what applies for one, applies for all. In fact, if competition does not grow, this type of measure may be necessary. It is not, however, ideal to regulate contractual agreements. It is more effective to open the market to forms of competition that would lead to the development of alternatives to Air Canada and its network. This is another factor in support of trade and ownership liberalization.

As it currently stands, the government needs to assess whether this provision is effectively creating a "level playing field" for independent carriers. If it is not, the government must be prepared to enact changes (ideally through liberalization, although imposition of an "MFN" policy is an option) as required to create a better environment for competition.

16.0 Recommendation on Joint Fares and Interlining:

- 16.1 That the Government of Canada monitor the development of third-tier competitive carriage in Canada, and assess whether the current provisions assist carriers sufficiently. Further, the Government of Canada should review other options to determine if there are additional actions it should take.**

Travel agent commission overrides and the right to negotiate as a group

Some issues that travel agencies face have little to do with the government regulations, Bill C-26 or the undertakings, so are not included in this section. However, they are germane to the growth of competition and consumer choice, and are reviewed in the section *Issues and Recommendations for Stakeholders*.

There are two areas of government involvement under existing provisions. One is in the “override” system, which determines how bonuses are earned, and the second is in the new ability for agents to negotiate collectively with Air Canada on the base commission rate.

The first decouples bonuses paid by Air Canada on domestic ticket sales from the sales themselves. Instead, overrides (bonuses) on domestic ticketing are tied into international sales. Many countries have similar provisions for their own carriers. This measure is intended to ensure that agents would book other domestic carriers. While this may be effective, the connection between international sales and domestic overrides may lead some agencies to book Air Canada on international flights to increase their domestic bonuses, compromising their neutrality and their efforts to select options based on consumer benefits.

The second suspends the “anti-collusion” provision in the Competition Act for travel agents so that they can negotiate as a unit. Although the process has been put into place, Air Canada has continued to reduce commissions it has been paying. As the right to negotiate has not led to a satisfactory conclusion for travel agencies, they have requested through their association, ACTA, that the government extend the provision to provide third-party arbitration.

It is difficult, and usually inappropriate, for the government to intervene in business-to-business matters. The market should sort itself out and result in a changed, but more viable and focused, travel agency community. However, there are a couple of open questions that may require a more substantive oversight.

As agencies move away from a model in which they are “agents” of travel providers to a fee-for-service agreement with travellers, they become an important tool of consumer information and choice. If the agency sector becomes unviable, a

potential source of unbiased information and data could be lost, and with it, an important resource for Canadian travellers.

The government should take action immediately in two areas. The first is to ensure that coupling international ticket sales with domestic bonuses does not have a perverse effect on consumer choice. The second is to review the government's Computer Reservation Systems regulations to ensure that the systems are "fair and neutral" in displaying, selling and presenting air service options. The CRS regulations were slated for review, but the process was delayed in the aftermath of September 11th. This review should also incorporate concerns expressed by the agency community regarding Web-only, consumer-only or other special fare categories and distribution mechanisms.

I do not support the agents' call for an arbitration process to be imposed by the government at this time, as a commercial agreement is best managed through the private, not public sector.

17.0 Recommendations on Travel Agency regulations:

17.1 That the Government of Canada review the domestic "override" program to ensure that it has no perverse impact on consumer choice.

17.2 That, to ensure fairness and consumer choice, the Government of Canada implement its review of the Computer Reservation Systems regulations, and ensure that the systems are "fair and neutral" and that the impact of Web-based fares and direct-to-consumer sales and pricing also be examined as part of the review.

Other Undertakings

There are a number of other undertakings still in effect. These include the transfer of surplus aircraft, surrender of airport facilities and release of slots (take off and landing times) at Lester B. Pearson International Airport, changes to the Chicago Formula (airport service costs allocation) among others. Anecdotally, although the processes have been slow in some cases, Air Canada has adhered to the requirements in the undertakings. No further action is recommended at this time. However, the government must monitor these undertakings and be prepared to modify or extend their enforcement period if competitive service has not grown enough to mitigate Air Canada's dominance.

Air Canada and the Official Languages Act (OLA)

There are a number of government measures in place to ensure that air travellers can be served in both official languages. Airlines usually provide services in both official languages, based on demand. All carriers are obliged, under the Aeronautics Act to ensure that safety briefings are given in both French and English (for aircraft with 20+ seats), and safety cards must have "pictographs" and bilingual wording. Airports with one million or more passengers a year must provide bilingual service and others are subject to the Official Languages Act (OLA) where numbers warrant (where demand for services in the second official language is at least five per cent).

Bill C-26 clarified Air Canada's linguistic obligation respecting subsidiaries, including those acquired in 1999 and 2000. Air Canada was made responsible for ensuring that CAC and all of Air Canada's other subsidiaries (such as the regional carriers) were able to serve the public in both official languages, with a timetable for implementation.

There are several aspects of how effectively Air Canada has complied with the provisions. The first is its record of serving Canadians in both official languages. The second is how effectively it is incorporating bilingual capabilities throughout its merged workforce. Third, there are the logistical and cost issues of retraining unilingual employees.

According to the Standing Joint Committee on Official Languages, Air Canada has had a history of difficulty adhering to the provisions, even prior to its privatization and CAC's takeover by Air Canada, although the number of complaints had decreased from 192 in 1992 to 137 in 2000, while during the same time, the number of passengers more than doubled. After the acquisition, the situation became difficult again, and the frustration level of passengers, the Commissioner of Official Languages and the Committee rose.

In recent months, Air Canada has announced a "Linguistic Action Plan" to improve its bilingual capacity. The plan includes deadlines for execution of its strategies as well as detailed actions and chain-of-command accountability. Additionally, Air Canada is working collaboratively with its unions to ensure successful implementation. With the exception of retraining, all elements of the plan are expected to be fully in place by 2003. Despite skepticism on the part of some observers, Air Canada seems committed to fulfill its obligations in that time frame.

Air Canada has already undertaken a number of initiatives. For example, it now informs passengers of their rights under the OLA in its in-flight publication, enRoute, and via its Web site. It has begun to use in-flight and telephone surveys to determine consumer satisfaction on bilingual announcements and service. It is considering other options for feedback systems as well.

Retraining is a more prolonged issue. Because of the need to replace workers on language training with other staff, the costs mount almost exponentially, and retraining is expected to take until 2010 to complete.

I sympathize with Air Canada's challenges and commend its "Linguistic Action Plan" and commitment to the OLA. However, I must also note the frustration voiced by the Committee over what it perceived as continued delays and an inadequate performance to date. Complete and satisfactory resolution to this ongoing issue will serve not only passengers, but Air Canada as well.

To ensure success, the government through its appropriate agencies must monitor Air Canada actions to ensure that its "Linguistic Action Plan" is implemented and that the deadlines contained therein are met.

18.0 Recommendation on Official Languages Act:

- 18.1 That Air Canada work to ensure the swift and successful completion of its "Linguistic Action Plan", which includes specific timelines, activities and objectives to increase bilingual capacity to improve bilingual services where required.**

Fair Treatment of Employees

The government's effort to ensure fair treatment of employees was accomplished by banning layoffs or relocation of unionized employees of Air Canada, Canadian Airlines or their wholly owned subsidiaries for a two-year period, which ended March 2002.

Although the specific provision has expired, problems with the merger of the two groups remain, and new issues are cropping up. The Canadian Industrial Relations Board (CIRB) recently ruled that the complex merger process to combine the two pilot groups at Air Canada and Canadian Airlines was flawed, saying that the merger protocol implemented by the arbitrator was unfair to former Canadian Airline pilots. Other unions that are still in the process of merging their seniority lists are watching the CIRB ruling, and its outcome, carefully.

On another front, four unions are now challenging Zip Air Inc., Air Canada's low fare/low cost subsidiary to have it declared a "common employer". Most contentiously, Zip wants to hire a single class of employee who can take on multiple roles as needed, serving as flight attendants, telephone sales agents, or at airport counters. Pilots have an agreement in place to fly Zip for reduced pay and different working conditions than at Air Canada. However, the agreement limits Zip to 20 aircraft.

As far as I can determine, labour relations between most carriers and their unionized employees have been a high-octane brew, and often adversarial. Mergers through their history have been highly emotional and never completely satisfactory to the partners: almost like a series of shotgun weddings. Mergers are over when the last employee from the previous regimes retires, and the divisiveness can last for decades.

Some people have suggested that the cost of, and limitations imposed on carriers, including Air Canada, by current collective agreements are the biggest obstacle in the way of achieving productive and responsive carriers. I think this is a bit simplistic. For one, even if the terms of the contracts become an issue, both parties signed the agreements, and it requires both parties to change them. For another, no serious problem is caused only by one factor. Likely, many other internal or operational issues get in the way of solutions as well. To lay the blame only at the feet of the unions may just set up a straw man and distract the carriers from dealing with all of their issues.

Now that the transition period has ended, government intercession in airline labour issues seems limited to the Canadian Industrial Relations Board. Fortunately, that body seems to be an effective method of dealing with concerns as they arise. No further intervention is recommended at this time.

Issues and Recommendations for Stakeholders

This section examines some ongoing challenges faced by stakeholder groups, and makes a few recommendations for action.

While I was not planning to make specific recommendations to stakeholder groups, not to do so would ignore a key piece in the airline-restructuring puzzle. If we are to solve the challenges that the airline industry presents, stakeholders must help design the solution. Their contributions are an untapped resource of potentially great power.

Stakeholder groups have different needs and interests; often differing within the individual groups themselves. A northern B.C. community has quite different needs and expectation of its air service than, for example, would Vancouver.

At the same time, there is also a great deal of commonality among the groups, depending on the issue. Access to low-fare travel is of equal concern to consumers and remote/rural communities, for example. The need for information and data is a concern shared by many groups.

As large as the “stakeholder” group seems, in reality, it isn’t large enough. There are a number of other bodies that are affected by the airline industry, and every attempt should be made to include them in the larger “community of interest”, including other government levels and departments.

Collective Action

Collective action by stakeholders is not only desirable: it is fundamental. In my conversations over the last two years, I was struck by the numbers of people who held that “the free marketplace will solve all of our problems” or that “government must take care of all our needs” as virtual articles of faith. In reality, neither business nor government can be relied on to provide all the answers. We must supply many of them ourselves.

In the early days of my investigations, I was also surprised how few stakeholders came together to share common concerns and solutions. Individual communities struggled on their own to learn how to react to the new environment, even though they experienced many of the same challenges, and could have benefited by sharing information. Within a significant number of communities, their meeting with the Observer was the first time that different stakeholders: provincial departments of transport, tourism, economic development, chambers of commerce, airports, travel agencies and consumers, came together as a group to discuss issues and solutions.

Recently, there have been signs that this is changing. The Air Transportation Association of Canada (ATAC), the Canadian Airports Council (CAC) and the

Tourism Industry Association of Canada (TIAC) have formed a coalition to address specific air issues. Provincial ministries responsible for tourism have been working together to develop solutions. Provincial ministries of transport are working on a Small Airport Viability Study. The Van Horne Institute brought together, for the first time, a number of academics and economists to collectively examine airline issues.

These initiatives should not only continue, they must expand. For example, many associations, such as the Federation of Canadian Municipalities or the Canadian Chamber of Commerce, have done extensive work on air industry issues. It would be useful for them to pool their information and knowledge by providing a clearinghouse of reports and positions, by holding joint meetings on airline issues or by doing both.

Another step would be to band together in a more formal way. For example, small community and airport issues are quite different from those of major centres, but are virtually identical across Canada. The same is true in the United States, and one of the stakeholder responses there has been the creation of the "Regional Aviation Partnership". According to its web site:

"Regional Aviation Partners (RAP) represents the interests of small communities, consumers, manufacturers, aviation vendors and the business entities that have a vested interest in regional airline service.

RAP is the industry's independent voice that truly represents issues faced by the regional aviation industry. Currently, we represent regional airline companies, aircraft manufacturers, state governments, airports, chambers of commerce, business organizations and hospitality organizations in 16 states and Canada, with representative populations exceeding 10 million people. RAP's members are the core of the organization's efforts to effectively lobby on small community air service issues at the federal, state and local levels of government."³³

A similar Canadian-based organization could serve the interests of small communities and regional carriers as well, and the interested parties should seriously consider this concept.

19.0 Recommendations on Collective Action:

19.1 That stakeholders use their associations to share information and resolve airline issues by building a "community of interest" approach to collective action.

19.2 That stakeholder associations work together to provide an information clearinghouse of reports, studies, positions, etc. related to airline issues.

³³ www.regionalaviationpartners.org

19.3 That stakeholders consider the horizontal approach taken by the U.S. Regional Aviation Partnership, to communicate collectively and to create broadly based advocacy positions.

Information and Data

Each stakeholder group, as well as government departments, has information or data that could assist others. A partial list includes:

- Provincial consumer protection laws and Small Claims Court processes
- Competition Act and Canadian Transportation Agency provisions
- Travel agents' knowledge of price changes, terms and conditions of carriage, consumer satisfaction/dissatisfaction, etc.
- Personal experiences of passengers

The need to increase information from airlines sources has already been discussed under "government recommendations". There is an additional need to improve access to individual stakeholders' information, and then bring together all the information for consumers and stakeholders at one "window" that is easy to access.

20.0 Recommendations on Information Sharing and Communication:

20.1 That stakeholder groups and provincial governments work with the federal government to assess what information each has that would be helpful in dealing with airline issues and creating a "single window" that could be accessed by all. This information should contain (but not be limited to) avenues of recourse for dissatisfied customers, passengers' travel experiences, pertinent travel agents' information, emerging issues, etc.

20.2 That stakeholders use their combined efforts to monitor changes in the airline industry, the effect of these changes on stakeholders and to provide government with independent analysis and recommendations.

Airlines

A professional and informed relationship between airlines and other stakeholder groups is essential if we are to articulate and resolve issues. Better information and communications is a first step.

Some of the issues between the carriers and other stakeholders are general. Many are specific to Air Canada because of its dominance and as the sole provider of regional-national-international network capabilities.

There are two areas of recommendation. The first concerns improving communications. The second looks at pricing issues.

Communications

It is not good enough to communicate reasonably well. Airlines have to be extraordinary communicators, at all times. Fees and surcharges add an unexpected and considerable cost to a ticket. Passengers give up a huge amount of personal autonomy, in exchange for "comfort and safety". Hundreds of dollars can be saved by changing the time or routing of an itinerary, but only if passengers know about it. Expensive packed items may require additional insurance, but only if passengers know what is and is not covered. The more passengers know what to expect, the better they can deal with air travel. Right now, airline consumers must also be activists, who can take nothing at face value, digging out information, comparing, asking, and checking. It is not simple, and it takes a great deal of time.

Better communications with other stakeholder groups such as communities, tourism or other business sectors is also important. Air Canada has made progress in this regard and has been talking with communities and provincial governments to provide a better understanding of what it can realistically be expected to deliver. It has also attempted on occasion to find alternative carriers in areas where it is leaving a community or route, even though it is under no obligation to do so.

Internally, it has recently merged the Provincial Government and Community Relations functions of Air Canada mainline and Jazz. This should make it easier for communities to get to the right person quickly. This is an important improvement, as communities reported difficulty in finding out who in Air Canada they should talk to, who had decision-making power, and having those people respond in a timely way.

Pricing

"Yield management" prices are another consumer irritant. Most people cannot comprehend why the price of a seat on the same flight can range wildly from thousands to a couple of hundred dollars. It has been called the "Airline Ticket Price Axiom" where complexity is fraud. If you cannot tell whether you are being fooled, you are being fooled.

AMR's legendary former president, Robert Crandell, recognized the problem ten years ago, saying:

Higher and higher full fares and an ever-growing array of discount fares surrounded by an ever-changing plethora of restrictions simply do not work. Business travelers, who have watched unrestricted fares skyrocket, have had enough.

"They are rebelling against a system they perceive to be unfair, which imposes unacceptable constraints on their ability to obtain a reasonable fare--like forcing them to stay away from home on a Saturday night. They're not shy about telling [airlines] how much they dislike the restrictions and complexity--and how stupid they think [airlines] are for having created something so unacceptable."

He then called for a new pricing system (Value Pricing), which would limit the dozens of fares on most flights to only four. His vision did not succeed. Ten years later, those same business travellers are rushing to the democratized world of low-fare carriers, with whom they can travel in relative comfort at lower (and fewer) fares with virtually no restrictions.

The full-service airlines are working with a pricing system that has become dysfunctional. Air Canada could put itself at the forefront of visionary change (to say nothing of increasing its good-will with passengers many-fold) if it was to embark on a review of yield pricing practices.

A separate issue that has come up recently is advertising that promotes "each-way" pricing in bold print. The smaller print says that only a round-trip ticket can be purchased (double the "big" print amount). In my mind, this is analogous to advertising a luxury car for \$15,000, and telling buyers in small print that an engine, wheels and windows are extra.

21.0 Recommendation on improving communications between airlines and stakeholder groups:

21.1 That the airlines publish and provide easy access (via their Web sites, in-flight publications, customer-comment cards) to the following information

- **Terms and conditions of carriage (tariffs)**
- **Avenues for consumer complaints both within the airline and via government provisions (Air Travel Complaints Commissioner, CTA, Office of the Commissioner of Official Languages with respect to Air Canada, etc.), including contact information**

21.2 While respectful of confidentiality concerns, that the airline community work with the Government of Canada and stakeholder groups to develop methods to collect more detailed and timely aviation data and create a dissemination program that provides needed information to stakeholders.

22.0 Recommendations on Pricing

- 22.1 That all carriers work to avoid consumer “sticker shock”, and ensure that advertised prices include the real costs to consumers, including fees, taxes and surcharges.
- 22.2 That carriers do not use “each-way” pricing when only a round trip ticket can be purchased.
- 22.3 That Air Canada work to first explain “yield” prices to consumers and then work with other international airlines to change the yield system into something that is understandable, rational and that consumers can trust.

Airports

Airports have become the front-line troops in the airline story. They sit squarely at the point where airlines, communities and passengers intersect. They must reconfigure their space for new security and policing requirements. They independently fund expansions, runways and in some cases, operations through user fees and are accountable to their Boards of Directors. They must follow Transport Canada regulations, and some must pay rent. They must develop themselves as an integral part of community life and development. They are also a key element in Canada’s national transportation infrastructure. It’s a lot to ask of one stakeholder group.

Airports of all sizes are challenged by declines in traffic, increases in costs, and in some cases, the extensive expansion programs launched prior to the economic downturn. Capacity reductions were felt most acutely in regional centres and some smaller airports may end up fighting for their very survival. Not all will make it.

For small airports that are within a reasonable drive of bigger centres, the problem is intensified. People will drive to the larger airport and avoid the connecting leg (and cost of the ticket) from their local airport. This is a double hit: first, airport revenues are reduced; second, since there is less capacity, it’s harder to get tourism traffic in, a potential economic loss to the community.

On the other hand, the post September 11th environment may help some small airports. Security line-ups and delays at bigger airports may increase the appeal of the smaller, easier to navigate ones. Private corporate jets may also use the smaller airports with lower fees and fewer hassles.

There has been a great deal of concern about airport viability. Communities fight to keep their airports and, when necessary, find the money to do so. New

infrastructure spending schemes have been touted recently, but there has been no mention so far of airports. The government, through the Airports Capital Assistance Program, provides some financing, but this is for capital projects only and cannot address operating deficits. Also, some smaller airports have raised issues with ACAP, saying that the program is not properly designed for their real world needs. A similar issue is that Transport Canada safety regulations are often very costly to the airport operations, and unnecessarily complex from the point of view of some airport managers.

Underlying the day-to-day issues is the original divestiture program. From airports' point of view, they were almost compelled into taking over airport operations from government. There were few established principles for setting fees, governance, and other fundamental matters. These were addressed on an ad hoc basis within contracts between government and airport boards. This was unsatisfactory for both airports and the government.

The federal government will soon introduce a Canada Airports Act, which will apply primarily to the government-owned, locally-operated 26 National Airport System (NAS) airports which handle 94% of all passengers and cargo, and to a limited extent to non-NAS airports. It will focus on issues related to accountability to the public and users, improved governance, principles for setting fees, oversight of subsidiaries and the requirement to respect Canada's international obligations as they affect airports.

The next few months and years will be challenging for airports as they redefine themselves in light of new legislation, and in the current uncertain environment. Many have taken on ambitious (in some cases, long overdue, in others, perhaps too ambitious) renovation projects, which are being paid for by passengers through Airport Improvement Fees.

In many cases, the improvements go well beyond runways and aprons: airports are retail and entertainment centres as well. In some airports, you can get a massage, tour a museum or stay at a hotel without stepping outside. You can buy lobsters, perfume, computers, booze, clothes, toys, books and CDs. In some airports, you can buy art. Airports are also responsible for safety: fire, police, medical. They are also, of course, now in the first line of defence against terrorist attacks. Airports also contribute to local economies, providing jobs and a link to the airline system. All of this goes far beyond the basic need to keep rain off your head while waiting for a flight.

Airports must be viewed in two parallel, but different ways: as a local hub and economic centre of a community, and as a cog in the larger wheel of the overall air system. It is little wonder that most communities want an airport, and feel that those that do have a huge advantage over those which do not.

How many airports do we need? It depends on one's point of view. If the airport is important as a generator of local economic opportunity, we probably have too few. If one just looks at the logistical requirements to move people efficiently in Canada, we probably have too many.

The challenge is to rationalize a system that has such differing demands placed on it. For a long time, various schemes have been proposed to put money back into the system: reappportioning of rents (a type of cross-subsidization), an expansion of ACAP, or even a new "small airports" strategy. Each of these (and other) solutions have their proponents and detractors, but there is a view that no matter what the government does, it has to do more, or at least do things differently, than it does now.

Urban, rural and remote communities

Airport issues are very often a part of broader community concerns. An airport is seen as an important way that the community links into transportation and trade, but the airport is only part of it. Communities want good connectivity, and an airline system that helps attract business and encourages tourism growth. In the best of all possible worlds, all communities would have local access to low-fare, competitive air service, with enough capacity to handle tourism travel peaks.

We don't have the best of all possible worlds, and smaller communities may never get all they want. However, there are ways to make the best of the world they have.

I have been struck by the maturation of community dialogue over the last two years. In August 2000, many of the conversations focussed on an expectation of "entitlements": that the government or Air Canada or both had an obligation to serve communities as part of "nation building". In more extreme cases, the conversation boiled down to "we want it, we need it, give it to us".

Happily, communities have shifted away from this unhelpful stance. They have become far more astute in articulating their needs, advocating for what they believe is right, and dealing with the airlines in a professional way. They are also creating their own solutions, following that old, but good truism: if you want something done right, do it yourself.

Charlo, NB tried to solve its local issue by having its airport run a small airline, Bay Chaleur. It didn't succeed, but the attempt was innovative and creative. Charlo had the foresight to understand that if you take a risk, you may fail, but if you take no risks, you are certain to fail. I hope that other communities see Bay Chaleur as a first learning step in air service "self-determination" and continue to seek local answers.

There are signs that communities are taking new approaches in other areas, too. Fredericton is looking to establish a "travel bank". Its business community would commit to a certain level of air service, and a carrier would serve Fredericton based

on that “guarantee”. It is an idea that has worked in a couple of American cities. Other Canadian communities are also considering establishing a “travel bank” as well.

Generally, the Canadian communities that are well positioned to deal with airline challenges are those that have permanent, or standing, air access committees. These groups are usually made up of representatives of the local chamber of commerce, airport, travel agents, tourism communities and the municipal government. They meet on a regular basis with carriers, build access strategies and advocate for their needs. This is one of the most useful actions a community can take, and I urge all of them that have not yet established working committees to do so.

Another positive action would be for communities to get together in articulating their positions, either through such existing associations as the Chamber of Commerce or Federation of Canadian Municipalities, or in an new, formal or informal process, such as the Regional Air Partnership detailed earlier.

23.0 Recommendations for Communities

23.1 That communities which have air access concerns establish a standing committee to deal with the issues, and to create access strategies for the community.

23.2 That communities, especially small communities, look for ways to unite, and create joint strategies and advocacy positions.

Travel Agents

Specific issues facing travel agents because of the acquisition by AC of CAC, and government responses, were reviewed in the section, *Travel agent commission overrides and the right to negotiate as a group*. However, that is only part of the story. Most of the challenges have little to do with the acquisition directly, but will have great impact on the future of travel agents, and their customers.

Travel agents were once simply “agents” of travel providers, including airlines, and received commissions from the providers. They were part of the distribution chain and as much as 80% of all tickets sold were through agents.

That has changed. Full-service airlines, including Air Canada, are reducing costs by reducing commissions. Internet ticket sales are booming. Agents have been forced to ask customers to pay for what was previously a free service: advice and ticketing. Customers can pay the fee for the expertise and ease of the transaction, or they can get onto a web site and do it themselves.

Then there was the events of 2001 – the tech. stock plunge, the economic slowdown, and the attack of September 11th led to a drop in all travel, including high-yield business. That made a precarious situation worse: accelerating the cost-cutting process and reducing volumes at the same time.

Not all agencies can manage the change. Some are being absorbed into larger agency chains and others are simply closing. Air Canada is concentrating its efforts on the agencies that provide the largest amount of sales, especially in business and long haul.

Conceivably, these changes could have a negative effect on consumers. Travel agents generally provide much more than simple ticketing. They price shop using tools and ticketing methods not always available on the web or directly to consumers. They can provide a great deal of information on the terms and conditions of the ticket, what the customer should be prepared for at the airport. They can take a lot of the “sting” of unpleasant surprise out of travel, and answer all questions quickly. They can find creative, alternate routings, especially on multi-stop or complicated itineraries, something that web sites cannot handle as well.

In summary, travel agents should plan to have an important, but changed role in the distribution chain, shifting their focus from travel providers to customers. There are many people who would think a service fee is money well spent if that fee provides them with quality service, good information and choice, and saves them time. People may trust the advice of an independent travel agent over an airline-based Web site.

Given the uncertainty in the marketplace, and the potential benefits the travel agency community can continue to provide, the government should continue to monitor the impact changes in the agency community are having on consumer protection and choice. The U.S. government was concerned enough about this issue that it established a commission to study the travel agency industry and information available to consumers on airline services.

Finally, travel agents have a great amount of data on travel that is booked. They also are the repository for great deal of informal, but very useful information on consumer concerns and issues: what they want, what they think of our current airline system, even their views on such thorny issues as “all in” pricing or the number and cost of add-ons.

24.0 Recommendations for Travel Agents

- 24.1 That travel agents ensure that the government understands their increasingly important role in providing consumer information and travel choice, and that appropriate government monitoring is put into place.**

24.2 That travel agents adopt a new and needed role as consumer advocates, providing neutral information and travel options in the best interests of the consumer, and to help consumers navigate the complex rules of airline travel.

24.3 That the travel agency community review the data that it collects, and develop, in cooperation with government and other stakeholder groups, a strategy to publicize portions of the data that can be useful in creating government policy, informing Canadians of the state of the airline industry, and measuring and monitoring changes in the airline industry.

Consumers

Most of the recommendations in this report should ultimately help consumers: the people on whose backs (and pockets) the whole system rests. Therefore, I do not have any direct recommendations for consumers.

I would, however, encourage airline passengers, and potential passengers, to understand and to use the considerable power they already have. At the end of the day, it is consumer action and spending that will determine if there is competition, if airlines fly to a community and if the quality of service is adequate.

If we want competition, we have to fly on competitive carriers. If we want high levels of service, we have to increase "demand" and get onto airplanes. If what we are getting is not good enough, we must exploit and exhaust every avenue of recourse open to us. Consumers retooled the North American automobile industry. Consumers forced "telecos" to a higher standard. We can as individuals, and collectively, do the same with the airline industry.

Summary of Recommendations

Long Term Recommendations

Air Policy

1.0 Liberalization

General:

- 1.1 That the Government of Canada create a new “made for Canada” policy framework to fully liberalize the competitive marketplace for air service to and within Canada, that serves to create an efficient and viable airline industry with strong domestic and international competitors and satisfies the needs of all Canadians.
- 1.2 That the government make every effort to reach reciprocal agreements, but be prepared to liberalize air service without direct or immediate reciprocal benefits for carriers, if there is an obvious advantage for Canadians and consumers, and when the liberalization has either no impact on the carrier industry, or when the carrier interests are clearly subsumed by a greater benefit.

Foreign ownership:

- 1.3 That, within the context of a liberalization framework, the Government of Canada liberalize the current rules of ownership to allow foreign-ownership of domestic Canadian carriers and a 49% ownership level of international carriers.

International Liberalization:

- 1.4 That the Government of Canada rigorously pursue and accelerate a program of liberalization under the bilateral regime.
- 1.5 That the Government of Canada work to achieve liberalized air agreements with key multinational partners and plan towards the establishment of common aviation areas.

2.0 Deregulation

- 2.1 That the Government of Canada continue to pursue its policy of domestic deregulation, and not re-regulate the airline sector in general or Air Canada in particular, and that it seek to deal with issues arising out of a market-driven environment by other and more effective means.

3.0 User Fees

- 3.1 That the Government of Canada act to ensure that the “all-in” price of airline travel is clearly and transparently communicated to consumers in advertising and promotional material, whenever possible, and that if certain fees or costs are broken out as separate items, (e.g. GST/HST) that there is clear justification or legal requirement to do so.
- 3.2 That the government monitor the proliferation and level of all fees, including the Air Traveller Security Charge to assess the cumulative impact of these charges on airline demand, especially short-haul and low-fare travel, and to take corrective action if necessary.
- 3.3 That the Government of Canada review its user-fee/user pay policies and tax structure imposed on the airline sector to ensure that these policies and charges are consistent with those in other transportation sectors.
- 3.4 That the Government of Canada include airport infrastructure in any major transportation infrastructure upgrade and spending program.

Transportation Policy

4.0 National Transportation Policy

- 4.1 That the Government of Canada’s Transportation Blueprint leads to the development of an integrated, equitably funded transportation system, and provides other jurisdictions the framework and vision to assist their long term planning, and that together, all levels of government work to achieve an efficient, safe, reliable and sustainable transportation system.

Government Policy

5.0 Air Access and Economic Development

Development

- 5.1 That, to more effectively serve the needs of community development, the Government of Canada separate economic development policy from transportation policy, by removing the declaration in Section 5 of the Canada Transportation Act of 1996.

- 5.2 That, when market forces are not sufficient, the Government of Canada expand the use of existing economic development tools and funding mechanisms to enshrine air access as part of these programs, and as a integrated element in community planning that contributes in a measurable way to overall development strategies.
- 5.3 That departments in the Government of Canada that have an interest in community access issues (e.g. Transport Canada, Industry Canada, Agriculture Canada, Human Resource Development etc.) work together, as well as with their provincial and territorial counterparts, to create common air access strategies based on local needs.

Regional Air Service

- 5.4 That the Government of Canada review all aspects of current transportation and taxation policies' impact on air service to smaller communities and on third-tier carriers, to ensure that the policies create an environment that encourages the growth and viability of these carriers. Changes or additions to policy should be made if it is found to be counter-productive to the development of third-tier carriage to small communities.
- 5.5 That the Government of Canada consider the option of a "small carrier" strategy that would encourage the growth of regional service.

6.0 Other Federal Departments and Other Levels of Government:

- 6.1 That the Government of Canada take the lead to establish new communications mechanisms between levels of government and other federal government departments whose policies or programs impact the quality and type of air service Canadians receive.

7.0 Data

- 7.1 That the Government of Canada pursue a policy of more open and accessible aviation data, building on its work of the Aviation Forum on Data, the subsequent "data gaps" analysis and the technologically-based pilot project.
- 7.2 That the Government of Canada enact appropriate legislation to collect detailed data on airline operations, particularly those data needed for government policy and oversight.

- 7.3 That the Government of Canada continue to work with stakeholder groups to develop a data strategy that clearly determines which data should be disseminated publicly, in what form and to serve what purposes.
- 7.4 That the Government of Canada accept that while the confidentiality of carriers' data should be respected whenever possible, the needs of this constituency must be balanced with the needs of the larger "community of interest" and with the potential benefits to the Canadian economy and communities.

Short Term Recommendations

Bill C-26 and the Undertakings

8.0 Protection from Price Gouging:

- 8.1 That this provision continue without change, but that the Government of Canada take measures to ensure timely and accurate judgements, and that success in this regard is monitored on an ongoing basis.

9.0 Protection of Service to Small Communities:

- 9.1 That the 120-day exit provision continue without change, but that the Government of Canada monitor its efficacy in the following areas:
- Outcomes of airlines' discussions with elected officials
 - Measurement of the appropriateness of the 120-day provision to ensure that it provides enough time for community action, but does not deter new entrants

10.0 Air Travel Complaints Commissioner:

- 10.1 That the Government of Canada continue the role of the Air Travel Complaints Commissioner, and that the Commissioner's work be monitored to ensure that complaints are handled in a timely and effective manner and that the Commissioner has all necessary powers.

11.0 Tariffs:

11.1 That the Government of Canada ensure that the complaint process relating to tariffs is easily accessed by consumers and is “user-friendly”.

12.0 “Passenger Bill of Rights”:

12.1 That the Government of Canada take no action to legislate a unique “Bill of Rights” for airline passengers, BUT

12.2 That the Government of Canada work with airlines, consumer groups and other levels and departments of government to provide “one-stop”, easily accessible information on what legal and regulatory tools are available to consumers.

13.0 Special Rules for the Airline Industry within the Competition Act:

13.1 That the government act on the concern expressed by the House of Commons Committee on Industry, Science and Technology and take action that will remove the special airline industry provisions from Competition law, and replace them with more appropriate and effective options as quickly as possible.

14.0 Anti-predation provisions:

14.1 That the Government of Canada closely monitor the cases before the Tribunal to ensure that the current criteria of “avoidable cost” and the Bureau’s new abilities under Bill C-23 are a fair, realistic and practical determination of anti-competitive behaviour in the airline sector, and to modify them, or take a new approach, if they are not.

15.0 Aeroplan:

15.1 That the Government of Canada ensure, that in the absence of competitive frequent flyer plans, this program is readily and fairly accessible to independent carriers that wish to participate.

15.2 That in the continued absence of competitive frequent flyer plans, the commitment is extended past its current deadline.

16.0 Joint Fares and Interlining:

- 16.1 That the Government of Canada monitor the development of third-tier competitive carriage in Canada, and assess whether the current provisions assist carriers sufficiently. Further, the Government of Canada should review other options to determine if there are additional actions it should take.

17.0 Travel Agency Regulations:

- 17.1 That the Government of Canada review the domestic “override” program to ensure that it has no perverse impact on consumer choice.
- 17.2 That, to ensure fairness and consumer choice, the Government of Canada implement its review of the Computer Reservation Systems regulations, and ensure that the systems are “fair and neutral” and that the impact of Web-based fares and direct-to-consumer sales and pricing also be examined as part of the review.

18.0 Official Languages Act:

- 18.1 That Air Canada work to ensure the swift and successful completion of its “Linguistic Action Plan”, which includes specific timelines, activities and objectives to increase bilingual capacity to improve bilingual services where required.

Stakeholder Recommendations

General

19.0 Collective Action:

- 19.1 That stakeholders use their associations to share information and resolve airline issues by building a “community of interest” approach to collective action.
- 19.2 That stakeholder associations work together to provide an information clearinghouse of reports, studies, positions, etc. related to airline issues.
- 19.3 That stakeholders consider the horizontal approach taken by the U.S. Regional Aviation Partnership, to communicate collectively and to create broadly based advocacy positions.

20.0 Information Sharing and Communication:

- 20.1 That stakeholder groups and provincial governments work with the federal government to assess what information each has that would be helpful in dealing with airline issues and creating a “single window” that could be accessed by all. This information should contain (but not be limited to) avenues of recourse for dissatisfied customers, passengers’ travel experiences, pertinent travel agents’ information, emerging issues, etc.
- 20.2 That stakeholders use their combined efforts to monitor changes in the airline industry, the effect of these changes on stakeholders and to provide government with independent analysis and recommendations.

Airlines

21.0 Improving Communications Between Airlines and Stakeholder Groups:

- 21.1 That the airlines publish and provide easy access (via their Web sites, in-flight publications, customer-comment cards) to the following information:
- Terms and conditions of carriage (tariffs)
 - Avenues for consumer complaints both within the airline and via government provisions (Air Travel Complaints Commissioner, CTA, Office of the Commissioner of Official Languages with respect to Air Canada, etc.), including contact information
- 21.2 While respectful of confidentiality concerns, that the airline community work with the Government of Canada and stakeholder groups to develop methods to collect more detailed and timely aviation data and create a dissemination program that provides needed information to stakeholders

22.0 Pricing

- 22.1 That all carriers work to avoid consumer “sticker shock”, and ensure that advertised prices include the real costs to consumers, including fees, taxes and surcharges.
- 22.2 That carriers do not use “each-way” pricing when only a round trip ticket can be purchased.
- 22.3 That Air Canada work to first explain “yield” prices to consumers and then work with other international airlines to change the yield system into something that is understandable, rational and that consumers can trust.

23.0 Communities

- 23.1 That communities which have air access concerns establish a standing committee to deal with the issues, and to create access strategies for the community.
- 23.2 That communities, especially small communities, look for ways to unite, and create joint strategies and advocacy positions.

24.0 Travel Agents

- 24.1 That travel agents ensure that the government understands their increasingly important and changing role in providing consumer information and travel choice, and that appropriate government monitoring is put into place.
- 24.2 That travel agents adopt a new and needed role as consumer advocates, providing neutral information and travel options in the best interests of the consumer, and to help consumers navigate the complex rules of airline travel.
- 24.3 That the travel agency community review the data that it collects, and develop, in cooperation with government and other stakeholder groups, a strategy to publicize portions of the data that can be useful in creating government policy, informing Canadians of the state of the airline industry, and measuring and monitoring changes in the airline industry.

Appendix I: Domestic, International and Transborder Markets

The Domestic Market

In August 1999, Air Canada and Canadian Airlines Corporation (CAC) flew 81% of total domestic **seat-kilometres**, compared with the (merged) Air Canada share of 73% in July 2002, a decline of eight per cent. Similarly, AC and CAC flew about 73% of the total domestic **seats** in 1999, compared with AC's share of 64% in 2002, a reduction of 11%. Overall, seats are down by three percent but seat-kilometres are up by five percent between 1999 and 2002. This means that capacity has been increasing on long-haul routes but decreasing on short-haul routes. This tends to suggest that most of the reduction in capacity when Air Canada took over Canadian Airlines Corporation was on short-haul routes.

The real changes are in the growth of WestJet and in low-fare seats overall. WestJet's share of the domestic market by **seat-kilometre** grew to over 14% in 2000 from 4.25% in 1999. When measured by **seat**, WestJet's share increased to 17% from 6.5%. All low fare capacity³⁴ by seat-kilometre increased to a 36% share in 2002 from 16% in 2000. At this rate of growth, a Transport Canada department official predicts that 50% to 60% of air services will be in a low fare format within the next year or two.

The number of city pairs served in Canada has increased slightly: from 219 served in July 00 to 222 in 02. There was also an increase in cities served by competitors to Air Canada, from 17 points receiving year-round service and nine receiving seasonal competitive service in 1999 to 24 year-round and 10 seasonal in 2002.

³⁴ Includes WestJet, Tango, CanJet, Jetsgo, Air Transat, Skyservice/Conquest

**Domestic operating statistics, market share by seat kilometre,
Daily Averages: Aug. 1999, July 2000, 2001, 2002**

	1999	% market	2000	%market	2001	% market	2002	%market
Air Canada	67,786,608	46.13	108,985,372	76.90	113,485,869	73.09	112,167,240	73.18
Canadian Airlines*	51,169,301	34.82						
Westjet	6,240,679	4.25	9,364,589	6.61	15,262,260	9.83	21,702,563	14.16
Canada 3000	7,811,382	5.32	7,159,757	5.05	17,781,273	11.45		
Air Transat	5,592,665	3.81	5,592,665	3.95	3,323,359	2.14	3,878,486	2.53
Royal	3,189,963	2.17	5,314,927	3.75				
First Air	1,918,538	1.31	1,822,166	1.29	1,862,728	1.20	1,839,255	1.20
Air Norterra	916,903	0.62	937,652	0.66	1,052,454	0.68	1,075,129	0.70
Skyservice							3,878,486	2.53
Jetsgo							3,789,486	2.47
CanJet							2,102,349	1.37
Air North							347,765	0.23
Other carriers	2,308,973	1.57	2540875	1.79	2492798	1.61	2492798	1.63
Totals	146,935,012	100	141,718,003	100	155,260,741	100	153,273,557	100
Total non-AC/CAI	27,979,103	19.04	32,732,631	23.10	41,774,872	26.91	41,106,317	26.82

*included in AC from 2000

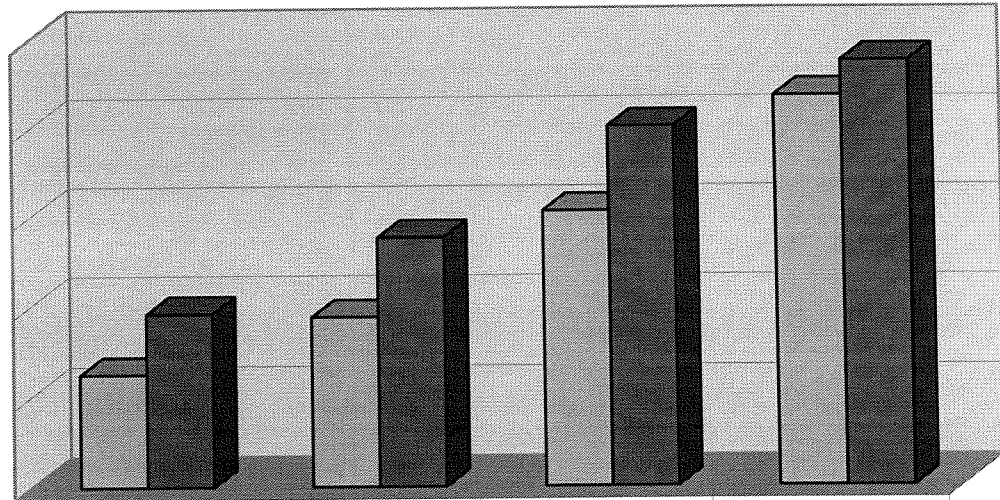
**Domestic operating statistics, market share by seat
Daily Averages: Aug. 1999, July 2000, 2001, 2002**

	1999	% market	2000	%market	2001	% market	2002	%market
Air Canada	60,606	40.98	94,466	70.30	93,427	65.28	88,700	64.25
Canadian Airlines*	48,746	32.96						
Westjet	9,571	6.47	13,804	10.27	20,024	13.99	23,666	17.14
Canada 3000	9,793	6.62	3,547	2.64	12,178	8.51		
Air Transat	2,687	1.82	2,687	2.00	1,634	1.14	1,374	1.00
Royal	2,063	1.39	3,867	2.88				
First Air	2,990	2.02	2,897	2.16	3,078	2.15	2,774	2.01
Air Norterra	959	0.65	969	0.72	1,127	0.79	1,081	0.78
Skyservice								1.646
Jetsgo							2,377	1.72
CanJet							2,606	1.89
Air North							336	0.24
Other carriers	10,477	7.08	12130	9.03	11657	8.14	13,493	9.77
Totals	147,892	100	134,367	100	143,125	100	138,053	100
Total non-AC/CAI	38,540	26.06	39,901	29.70	49,698	34.72	49,353	35.75

*included in AC as of 2000

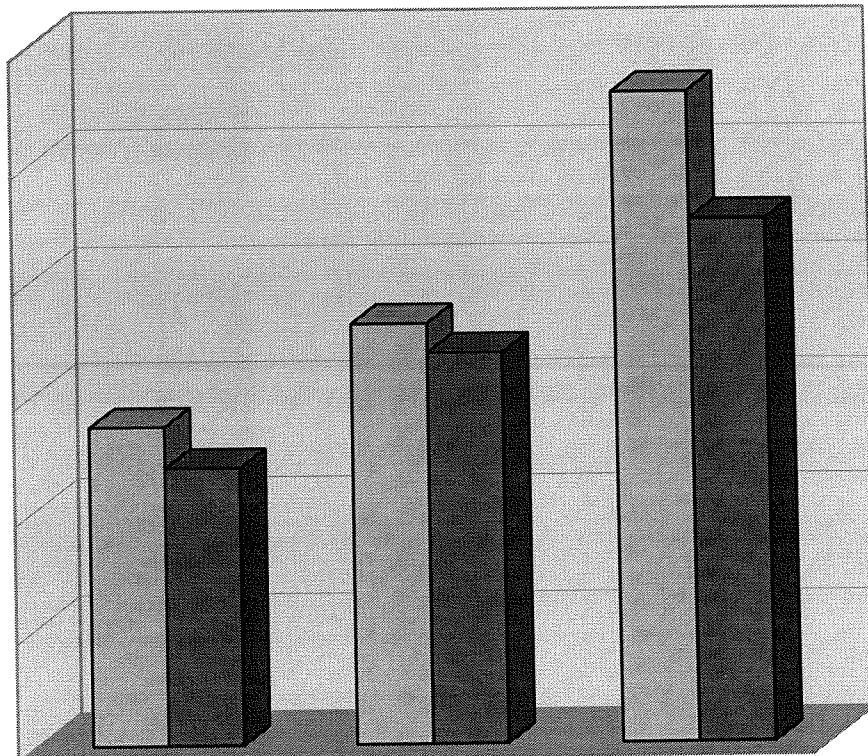
Number of Domestic City-Pairs Served						
Major Scheduled Airlines						
July 2000, 2001 and 2002						
Airline	July 2000		July 2001		July 2002	
	Total	Daily*	Total	Daily*	Total	Daily*
Air Canada**	145	142	143	137	139	134
WestJet	26	25	38	35	53	36
Canada 3000	20	6	25	17	--	--
Air Transat	11	2	11	1	9	1
Skyservice	--	--	--	--	8	5
CanJet	--	--	--	--	7	7
Jetsgo	--	--	--	--	6	4
Royal Airlines	17	6	--	--	--	--
TOTALS	219	181	217	190	222	187
Notes:						
*- Number of city-pairs with at least 5 weekly roundtrip flights.						
**- Air Canada includes operations by Tango and the wholly-owned affiliates						

Growth of WestJet 1999 - 2002 Daily Averages



	1999	2000	2001	2002
■ Seat Kilometres(millions)	6,240	9,364	15,262	21,702
■ Seats	9,571	13,804	20,024	23,666

Growth of low-fare capacity 2000 - 2002 Daily Averages



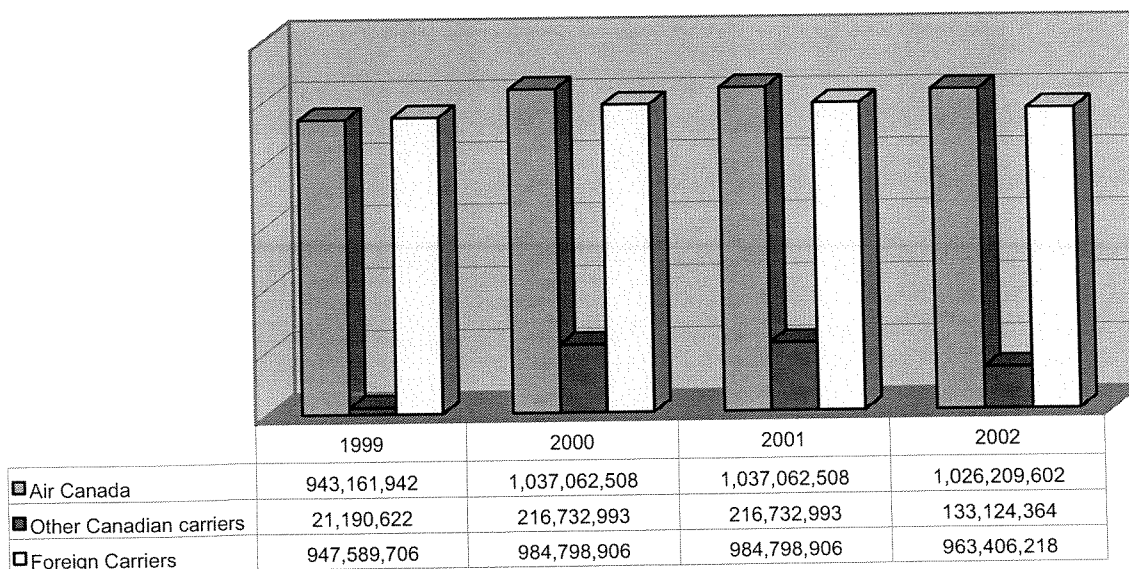
	2000	2001	2002
■ Seat Kilometres (millions)	27,273	36,095	55,770
■ Seats	23,688	33,556	44,971

The International Market

*PLEASE NOTE: The statistics quoted in this section, and the subsequent section, **The Transborder Market**, DO NOT include charter services, which are generally based on seasonal demand. While charter carriage has had an effect on the amount of capacity available to travellers in some parts of the country, the purpose of these sections is to compare levels of year-round scheduled service offered in Canada.*

International service has also seen change between 2000 and 2002. The major shift is the loss of Canada 3000, which flew 132 million seat-kilometres to international destinations in 2001. No Canadian carrier replaced the capacity. The jump in "other Canadian carriers" between 1999 and 2000 includes Canada 3000 and Air Transat in "scheduled service" statistics for the first time. Air Canada's share is virtually the same as the combined AC/CAC number prior to the purchase of CAC by AC: 49% for the two carriers in 1999 vs. 48% for the merged Air Canada in 2002. While Air Canada does have slightly less than half of the international market, there is no Canadian competitor who comes a close second. In 2002, Air Transat was the only

**International Operating Statistics Scheduled Service
Weekly Averages 1999 - 2002 by seat-kilometre**



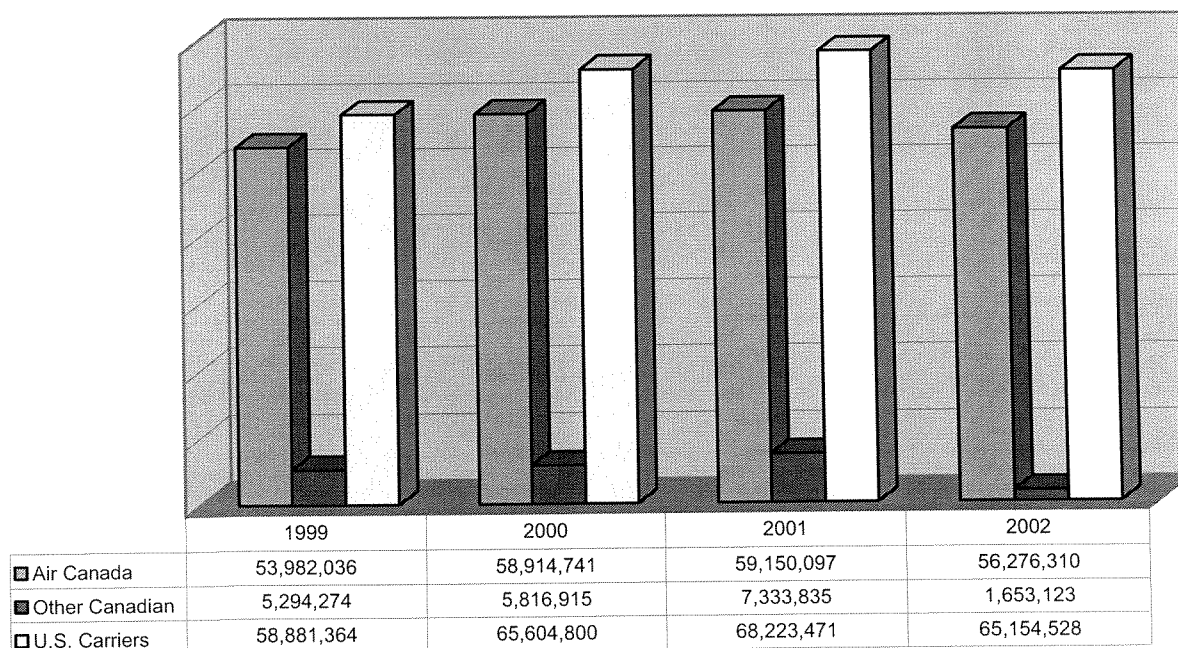
other Canadian-owned carrier that flew international routes, and it held just over six percent of the market. Thirty-five foreign carriers in Canada served the remaining 46% of the market.

The Transborder Market

Transborder service is almost identical in shape to international, except there are even fewer Canadian competitors. In 1999, Air Canada and Canadian Airlines Corporation had a combined share of 46%. In 2002, the merged carrier has 48% – slightly stronger than four years earlier. Other Canadian carriers hardly exist in the transborder market – four per cent in 1999 and a paltry one per cent in 2002. U.S. carriers picked up the difference in 2002, with eleven U.S. carriers and their affiliates controlling 53% of the market by seat kilometre.

This state of affairs may change for the better with WestJet's recent announcement to launch transborder services.

**Transborder Operating Statistics Scheduled Service
Daily Averages 1999 - 2002**



Appendix II: Meetings Held/Input Received

This list represents the key stakeholders with whom I met from August 2000 to July 2002. It does not indicate multiple meetings, nor does it list each individual.

Abbotsford Airport Authority	Capital Canada Ltd.
Air Canada	Chamber of Commerce Transport Committee
Air Canada Regional	Charlesbourg, QC
Air France	Charlo, New Brunswick
Air Labrador	Charlottetown, PE
Air Line Pilots Association	Chartered Institute of Transport in North America, Ottawa Chapter
Air Transport Association of Canada	China Airlines
Air Travel Complaints Commissioner	Clark & Company
Airport Council International	Commissioner of Official Languages
Alberta Hotel and Lodging Association	Competition Bureau
American West airlines	Council of Concerned Airport Users
Air Transat	Council of Tourism Association of British Columbia
Association of Canadian Travel Agents	Dr. David Gillen
Atlantic Airports Council	Dr. Dyane Adams, Commissioner of Official Languages
Atlantic Canada Airports Council	Dr. Tae Hoon Oum
Avalon Convention & Visitor Bureau	Economic Development Edmonton
Avia Marketing Consultants	Edmonton Airport Authority
Aviation sub-committee (provincial/territorial transportation departments)	El Al Airlines
Barry Prentice, U. of Manitoba	Factor 60/70 CAI Retirees
Bathurst, New Brunswick	Federation of Canadian Municipalities
Bearskin Airlines	First Air
Calgary Airport Authority	Fred Lazar
Calgary Chamber of Commerce	Fredericton, NB
Calgary, AB	Gander, Nfld. & Lab.
Canada 3000	Government of Alberta
Canadian Airports Council	Government of British Columbia
Canadian Association of Visitors and Convention Bureaus Meeting	Government of Manitoba
Canadian Auto Workers	Government of New Brunswick
Canadian Chamber of Commerce	Government of Newfoundland and Labrador
Canadian Corporate Travel Agents	Government of Nova Scotia
Canadian Federation of Independent Business	Government of Nunavut
Canadian Owners and Pilots Association	Government of Ontario
Canadian Tourism Commission	Government of Prince Edward Island
Canadian Tourism Commission (Research)	Government of Québec
Canadian Transportation Act Review Panel	Government of Saskatchewan
Canadian Transportation Agency	Government of the Northwest Territories and stakeholders]
Canadian Transportation Research Forum	Greater Halifax Conventions & Meetings Bureau
Canjet	Greater Quebec Area Tourism and Convention Bureau

Halifax Chamber of Commerce	Royal Air
Halifax, Nova Scotia	Rural Secretariat (Canadian Rural Partnership)
Hawkair	SABRE Reservations System
HeliJet International	Saskatoon Airport Authority
Hospitality Newfoundland and Labrador	Saskatoon, SK
Hotel Association of Canada	Shawn Murphy, M.P.
House of Commons Standing Committee on Transportation and Government Operations	Signature Vacations
Icelandair	SkyComm Air Management Ltd.
Iles de la Madeleine, QC	Skyservice (RootsAir)
InterGlobe Technologies	St. John's NF Airport Authority
International Association of Machinists	Statistic Canada
Japan Tourism Bureau	Terrace, B.C.
Kitimat, BC	Territory of the Yukon
Labrador City, NF	The Honourable Senator Lise Bacon, Chairperson of the Standing Senate Committee on Transport and Communications
Labrador North, Newfoundland	Toronto, ON
LPS Aviation	Tourism & Technology Conference
Manitoba Aviation Council	Tourism Air Policy Forum
Manitoba Chamber of Commerce	Tourism British Columbia
Miramichi, New Brunswick	Tourism Calgary
Montréal, QC	Tourism Industry Association of Canada
Mr. Ovid Jackson, M.P., Chairman of the House of Commons Standing Committee on Transportation and Government Operations	Tourism Industry Association of New Brunswick
Newfoundland/Labrador Department of Transportation	Tourism Industry Association of Nova Scotia
Nova Scotia Air Access Committee	Tourism Industry Association of PEI
Nova Scotia Dept. of Transportation	Tourism Industry Association of Yukon
Office of Official Languages	Tourism Saskatchewan
Oneworld Alliance	Tourism Toronto
Ottawa Visitors and Convention Bureau	Tourisme Montréal
Pacific Coastal Airlines	Transport 2000
Policy Shop	Transport Canada
Policyshop.com	Transportation Association of Canada Aviation Subcommittee
Premier of Yukon	Travel Alberta
Prince George Airport Authority	Van Horne Institute Air Policy Meeting
Prince Rupert, BC	Vancouver, BC
Province of Alberta	VIA Rail
Provincial Airways	Virgin Atlantic
Provincial/territorial tourism ministers	Wabush, NF
Public Interest Advocacy Centre	WestJet
Québec City, QC	Whitehorse, YK
Québec Tourism and Aviation Forum	William Clarke
Regina Airport Authority	Winnipeg Airport Authority
Regina, SK	Winnipeg MB
Rick Erickson	Yukon Convention Bureau
Robert, Deluce, Deluce Capital	

Appendix III: Mandate of the Independent Observer

From August 2000, and continuing for a period of 24 months, the Independent Transition Observer has reviewed the impacts of airline restructuring on stakeholders and assessed whether the airline industry is healthy and competitive and meets the needs of Canadians.

In particular, the Observer has:

- Considered the views of consumers, urban, rural and remote communities, travel agents, airports, airlines and airline employees;
- Assessed whether Transport Canada, the Canadian Transportation Agency and the Competition Bureau responsibilities relating to airline restructuring are clear and being carried out appropriately;
- Considered whether the government's monitoring measures are adequate;
- Assessed industry support to the measures introduced in Bill C-26, including the commitments and undertakings of Air Canada to the Federal government;
- Assessed Air Canada's linguistic obligations; and
- Assessed the need for a Passengers' Bill of Rights.

Interim reports were produced every six months with one final comprehensive report to the Minister. Reports are available on the website, www.tc.gc.ca, follow the links on "airline restructuring". The final report includes recommendations on monitoring and related airline restructuring matters.

Debra Ward, the Independent Transition Observer was appointed by David Collenette, the federal Minister of Transport on August 1, 2000. She is an Ottawa consultant specializing in communications and policy strategies relating to tourism and travel issues. She has served on a number of national and international boards and committees and federal government advisory committees for the Auditor General, the Minister of National Revenue, the Minister of International Trade and the Canadian Labour Force Development Board.

Formerly President of the Tourism Industry Association of Canada, Debra has done extensive work on policy issues relating to the impact of the Canadian transportation system on communities, small and medium-sized businesses and the economic and social well being of Canada and Canadians.

Afterword and Acknowledgements

This report is the final effort of the Independent Transition Observer on Airline Restructuring, to put some shape to the extraordinary changes in the airline sector, and the effect of those changes on, what are formally called “stakeholder groups” but are more accurately but less formally, simply Canadians who are deeply concerned with the impact the airline industry and government policy has on their future.

I have met with dozens of community and stakeholder groups across Canada, listened to their concerns and suggestions, and finally in this report, made my own recommendations that I hope support our collective goal to achieve a healthy airline industry that serves the interests of Canadians.

To those of you with whom I did not or could not meet, I apologize. To those who have different solutions to those I present here, I hope that I have at least captured your points of view honourably and fully, within the four reports that I have submitted. Disagreements between people of good will are not only acceptable, but also essential if we are to continue a meaningful dialogue, and achieve reasonable solutions. I hope that these debates will continue in other forums.

There are many people to whom I owe large debts of gratitude, starting with David Collenette, the Minister of Transport. I have found Mr. Collenette to be an informed and knowledgeable Minister, respectful of different points of view, including my own, and always ready not only to debate and defend, but also to listen. I thank him for the trust he has shown in me throughout this process and through some very difficult times. He has ensured that the word “Independent” in my title was an article of fact, and respected it. He “knows his files” as they say in Ottawa, and that is high praise indeed.

I must also thank the many people within Transport Canada who have always been ready to provide me with information, historical contexts, and details, but never tried to influence my lines of investigation, my reports or my final recommendations. Special and sincere thanks to Louis Ranger, Valérie Dufour, Eric Mainville, Roger Roy, Elizabeth Dixon and all the others who provided support. Special gratitude goes to Brian Carr, who fielded the majority of my demands and questions, and always with alacrity and unflinching good humour. Similar thanks to Gavin Currie and others in the CTA who helped me navigate the complex world of transportation regulations, Konrad Von Finckenstein, and others at the Competition Bureau, Dr. Dyane Adams and others at the Office of the Commissioner of Official Languages, among many other individuals. If I haven’t mentioned someone by name, it is only lack of space, not lack of appreciation.

I must stop here to say a word about “bureaucrats” and “bureaucracies”. Over the last two years, I have grown to know many of these people fairly well. Their knowledge of the aviation sector, their internal debates to find the “best” policies and the gravitas with which they approach most challenging issues was unbounded. Their concern, professionalism and expertise shame those who have accused the government of being monolithic, unresponsive and short sighted. The reality is anything but.

Thanks also go to the many colleagues and friends both within the aviation community and without, who have provided expert information, advice and debate. Special thanks to those who helped me learn more about the aviation sector. If I have evolved to an

informed observer from just an observer, it was because of all of the many people, with far more expertise than I can ever achieve, who were so willing to get me through "Aviation 101". Many of these people who started as colleagues and acquaintances I also now consider friends.

Thanks also to many people in the airline industry itself who were equally unstinting of their time. They have extraordinary loyalty to their airlines, and are fearless in the face of poor odds and new challenges. There have been many "Monday morning airline quarterbacks", including myself, all of whom have the "answer" to fix management, especially Air Canada's management. And, while Air Canada may have made a lot of mistakes, it's not as easy to run an airline as it looks, or else we'd all be doing it, and everyone would make money.

On a personal note, I have to thank my family, who endured two years of my quixotic journey as the Independent Observer, and dealt with my frequent absences and my absent-mindedness when I was home. My love and thanks to Siobhan, who did her four-to-six year old best to understand that Mummy travels a lot because she does something to do with airlines. Thanks also to my mother-in-law, Merle, who took such good care of Siobhan, and helped us keep it all together. My last and most deeply felt thanks go to my husband John, for handling all the child-rearing duties and thousands of other reasons beside.

Finally, although my job has ended, the story of airline restructuring goes on. But we have accomplished much and learned much. I urge everyone to continue to debate, to strive to find ways to make the airline industry work for Canadians.

And, I will continue to watch as this fascinating and challenging sector re-invents itself yet again. It was a privilege to be a small part of it for a short time, and I wish the airline industry, and all of those who rely on it, a prosperous and safe journey.

*Debra Ward
Independent Transition Observer on Airline Restructuring*