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# Airport Policy in Canada

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# Executive Summary

Historically, Canadian airports began as municipal creations with federal oversight in safety, emergency landings and in the creation an airway spanning the country. The poor state of post-Depression airports and the intensive federal involvement in airports during the war years (1939-45) combined to create a natural shift in airports from municipal entities to federal operations. A transformative change in 1992 resulted in airport transfers from the federal government to self-financing, not-for-profit corporate entities making leasehold payments to the federal government.

The survey and construction of the Trans-Canada Airway represented one of the largest federal initiatives in Canadian history. The dramatic growth in the airline industry in Canada would not have taken place without it. The resulting benefit to the movement of persons and goods allowed great strides forward for the country.

This paper will assess whether the not-for-profit model of 1992 was accompanied by any similar grand design and whether it has in any way addressed the needs of the airlines, the travelling public, cargo and, ultimately, the Canadian economy.

The paper will examine airport policy in Canada, the United Kingdom and the United States, including underlying issues of traffic levels, landing fees, commercial airport operations and competition. It will question whether productivity, transparency, accountability and pricing have been achieved under the not-for-profit model. The paper concludes that the not-for-profit model has constrained rather than enhanced growth and represents little more than an intermediary step before privatization. With the wide benefit and limited criticism of privatized airports, the model best suited to the growth of airports and the economic growth of Canada is a privatized airport model.

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CALGARY, AB. (1940s)



## I History of Canada's Airports

After World War I, many decision-makers initially perceived aviation as war-related and poorly adaptable to peacetime Canada. The Minister of Reconstruction reflected that mood in his December, 1918 claim that he "did not think that Canada would ever have need for an air service."<sup>1</sup>

In *The History of Canadian Airports*, author Tom McGrath claims that the large number of pilots returning from overseas, the market for surplus aircraft and the potential for air exploration of the remote northern regions of Canada all contributed to more progressive thinking about aviation. When Canadian Pacific Railway applied in February, 1919 for legislation to extend its charter to include aircraft operation, it demonstrated a clear private interest, which in turn hastened government action. The *Air Board Act*—drawn heavily from precedent in the United Kingdom—became law in June, 1919.

Created under that *Act*, the Air Board was mandated to set policy in aircraft and airport development. Within the year, the Air Board had published a paper delineating government policy in aeronautics and establishing the initial framework for airports. Steeped in post-war thinking, the paper not only urged Canadians to remain ever-mindful of the threat of war, it showed a marked reluctance toward public funding both for airports and for commercial aviation development.

The Air Board pointed out that public attention to Blériot's first flight across the English Channel in 1909 quickly dissipated with the threat of war and aircraft design immediately re-focused to meeting war requirements. Since commercial aviation had not advanced in the ten years since that first flight, the Air Board concluded that post-war Canada was ill-prepared for air transportation beyond "belligerent purpose."<sup>2</sup> The commissioners stated that "a completely new orientation" in the design and manufacture of aircraft was required. The Air Board recommended that Parliament not commit "the money, equipment and facilities necessary to do the pioneer commercial work". Their fear was that stagnation could potentially occur under a government model of commercial air development.

The Air Board recommended against federal airports, urging municipalities, towns and cities to establish airports themselves. The commissioners reasoned that "an urban municipality without an aerodrome will not be on the air map"<sup>3</sup> The Board carved out a federal presence at municipal airports in the regulation and

monitoring of emergency landings, safety, meteorological services and standards. It limited the federal government to the establishment of air routes and to the construction and maintenance of federal airports.<sup>4</sup>

Importantly, the Air Board urged a distinct federal presence in the exploration and survey of the vast Northern regions of Canada. That policy, states McGrath, resulted in the development of a commercial northern air service and in the discovery within ten years of more information about Canada than had been learned in the previous three hundred years. The commitment by the federal government to the northern region initiative led quite naturally to the next stage, mail delivery by air.

Yet, the continued use of Canada's lakes and waterways by seaplanes and flying boats stalled the development of commercial aviation and airports. In 1923, the Air Board was disbanded and the few existing federal airports were placed under the jurisdiction of the Department of National Defence. Although its initial concern was the increase of military air travel budgets rather than commercial aviation, the Department's 1927 renowned 'flying club initiative' kick-started both commercial aviation and airports.

The Department of National Defence offered incentives to groups who could provide an airport, a hangar, an instructor, an engineer and thirty members willing to learn to fly. In return, the Department would grant the airport two airplanes and a \$100 grant to each successful licensee. The 'flying club initiative' was wildly successful and by 1928, there were sixteen established clubs and eight more the following year. As a result, airports sprang up across the country providing a growing fleet of trained pilots ready and eager for commercial air service. All that remained to advance Canadian commercial aviation was a coast-to-coast airway that would provide intermediate airports and landing fields. In 1927, Government estimates suggested a cost of between \$5 and \$6 Million to establish a Trans-Canada Airway.

With United States air transport providers nipping at the heels of the nascent Canadian air industry, Canada moved to survey the proposed airway.<sup>5</sup> The government undertook the survey in 1928 and by 1929, construction of the Trans-Canada Airway had begun, initially establishing intermediate airfields every 30 miles between Winnipeg, Calgary and Edmonton. A 1932 Order-In-Council authorized the Canadian government to establish work camps to employ "single, homeless men" to clear, stump and grade the airfields in exchange for food, camp lodging and wages of \$1 per day maximum.

With construction underway, the Minister of National Defence took to the air waves to explain the project to Canadians, proudly claiming that: "When the Trans-Canada Airway is completed, it will bring about a revolution comparable in our generation to that achieved by the Fathers of Confederation in the building of the Intercolonial and Canadian Pacific Railways."<sup>6</sup>

By 1936, the relief camps had been disbanded and the final work contracted to private companies. Installing radio range beacons in the mountains, making radio upgrades and improving lighting at airfields across the country completed the Trans-Canada Airway and heralded a new era for Canada.

■ ■ In 2000 Transport Canada admitted that for the previous sixty years they had been making ad-hoc decisions on airports.

Yet, many of the municipal airports originally recommended to be part of the Trans-Canada Airway had fallen on hard times during the intervening Depression years and were well below government standards. In response, the federal government announced that it would contribute up to one-third of the cost to upgrade airports. Vancouver, Lethbridge, Regina, Winnipeg, Toronto and Hamilton were upgraded, while the government negotiated with other airports.

Some municipalities, notably Montreal, Ottawa, North Bay and London, refused to participate in the upgrades of their airports. The *Trans Canada Airlines Act* of 1936 allowed the federal government to assume the entire cost of developing non-participating airports.

On April 1, 1939, Canada's first commercial flight followed the new Trans-Canada Airway. Billed as a "fast, daily, time-saving service on the world's fastest commercial plane with normal flying speeds of up to 180 mph,"<sup>7</sup> the twin-engine 10-seat Lockheed Electra flew between Montreal and Vancouver in 15 hours, with 6 intermediate stops. The initial fleet of Trans-Canada Airlines consisted of two Lockheeds and a biplane. For the first year of the flights, at each stop hundreds of Canadians flocked to witness the silver transcontinental wonder. Often, the Minister of Transport, C.D. Howe, would tag along on the flights.<sup>8</sup>

When World War II began, the Canadian government was front and centre in its ability to provide viable airports for training. Under the British Commonwealth Air Training Plan, the Department of Transport was given jurisdiction to select and build airports. Airports that had been part of the Trans-Canada Airway were brought into the programme and suitable municipal airports were leased, upgraded and expanded by the federal government. By the end of the war, an astonishing 149 new airports had been built and 73 existing facilities had been expanded. However, many of those airports were still under lease agreements with their municipalities, resulting in joint government ownership. This compelled the Department of Transport to recommend that:

1. The number of airports should be maintained. The Department felt that the greater the number of airports, the greater the demand for aircraft with Canada benefiting in the anticipated increases in manufacturing, operations, maintenance and employment.
2. Appropriate airport standards should be established to ensure the survival of commercial air, with future upgrades at federal government expense.
3. If municipalities were unable to manage the airports, they should be transferred at no cost to the federal government.

In 2000 Transport Canada admitted that for the previous sixty years they had been making ad-hoc decisions on airports. This, they claimed, was due to an absent “coherent vision of an airport system to guide decision making.”<sup>9</sup> The lack of a coherent federal policy may explain the post-war recommendation to assume responsibility for municipal airports and to maintain excess capacity.<sup>10</sup>

Airports that remained under the jurisdiction of their municipalities were still eligible for federal subsidy. Besides a capital subsidy, there were operating subsidies that ranged from 1 cent to 5 cents per square yard of paved surface. Increasingly the subsidies were insufficient to meet airport requirements and, by 1953 the federal government began adding new ad hoc grants, one being based on the airport’s square footage of public space. In 1958, a new policy established five different types of airport (main line, satellite, local, remote or development), with grants awarded contingent upon classification. Policy in 1965 addressed the need for smaller airports.


By 1972 the five classifications were reduced to two: national and community. The federal government subsidized both types, but subsidies to community airports were capped at \$2-million per year, an amount insufficient to meet airport requirements. Community airports then turned to their provincial governments for support, with the result being wide-ranging differences in financial support to airports across the country.<sup>11</sup> Some upgraded community airports were transferred back to the national system.<sup>12</sup> Unable to meet even the committed funding for 1972, let alone the new upgrades the community airports required, Treasury Board requested a new airport policy. By 1979 the federal government set the community airports adrift, maintaining funding only to the national airports.

In 1982, after a four-year funding hiatus, the federal government once again financed community airports for a brief time, basing funding on the ability of each airport to spur secondary industry in its community. Yet, funding for both national and community airports fell far short of paying for the required upgrades, putting their very survival at risk.

Transportation economist Dr. Mike Tretheway commented on the state of Canada’s airports at that time.

“Old folks like me need to think back to how awful the airport system was in the 1980’s. I remember the terminal in Ottawa, for example, where you could hardly move. We had severe runway congestion in both Vancouver and Toronto with aircraft sometimes waiting for as long as an hour. Runways were needed. We had hopelessly crowded terminals. In Vancouver during the Asian peak, it was almost impossible for people to get to their gate because there was too little space in the old terminal. At Toronto, Terminal 1 was falling apart and Terminal 2 needed major repairs and replacement. I remember arriving at the Edmonton airport where once they had to turn off the escalator because the arrival hall was so congested. It was discovered that the Moncton airport had seven layers of roof, all rotting, and a runway that often could not be used because of the damage. The Comox airport was underserved and had essentially what was almost a trailer for an airport terminal. Montreal and Edmonton had split their traffic into two airports and their markets suffered as a result.”<sup>13</sup>




 In 1987, Transport Canada recommended the transfer of airports from federal government support to not-for-profit authorities.

Exclusive of air traffic control, the federal government had been subsidizing airports at approximately \$500-million per year, of which half was returned by a tax on airline ticket sales. The 1985 federal budget questioned whether the government could remain financially committed to airports in light of budgetary concerns.<sup>14</sup>

Studies by the International Civil Aviation Organization (ICAO) and the International Air Transport Association (IATA), the industry standard-bearers, show that the number of airline passengers grows at double the rate of world economic growth; cargo grows at three times the rate. Consequently, there exists a continuous strain on airports to expand to meet demand. A government owned airport model is a poor fit to endless demands for increased funding to pay for airport expansion. The poor state of Canada's airports by the 1980's reflected that strain.

By 1985, the combined efforts of the Neilson Task Force policy paper, *Freedom to Move* and the federal budget created momentum toward a new era of self-sustaining airports. In 1987, Transport Canada recommended the transfer of airports from federal government support to not-for-profit authorities.

In 1987, the privatization of the British Airports Authority by the British Cabinet of the Right Honourable Margaret Thatcher was met with critical acclaim. Without existing data or empirical evidence in favour of the for-profit option, the Canadian Government did not pursue it. Nor did Canada pursue the U.S. model with airports operated and taxed by local governments. Concerns regarding airline bonds and the perception of undue influence by the airlines in airport development and in competitive issues rendered this model unattractive.

Rather, in 1987, the Canadian government took a cautious first step by transferring airports from its jurisdiction to that of Local Airport Authorities (LAAs), allowing each airport to "opt-in" on a voluntary basis.



## II. Canadian Airports 1992- the Present

The transfer of Canadian airports took place under the watch of two separate governments. The Mulroney Conservative government created the Local Airport Authorities (LAAs) in 1987. Chrétien's Liberal government established policy under the *National Airports Policy* of 1994 and created the Canadian Airport Authorities (CAAs). During the 1993 federal election campaign, the proposed transfer of Pearson International Airport became a significant issue between the Conservatives and the Liberals, contributing to the defeat of the Conservative government. Eventually, the Pearson Airport controversy led to a broader examination of airport transfers and, although the transfers under the LAA system generally were viewed as positive, the lack of an underlying airport policy undermined the overall system.

The LAAs were established by government announcement in April, 1987 of a "new direction for airports". If a local community expressed interest, then management of the airport would be transferred from Transport Canada to an LAA. The four major airports that opted into the LAA system were Montréal (Dorval and Mirabel counting as one airport), Vancouver, Calgary and Edmonton. Under the Local Airports Authority of 1992 and the Canadian Airports Authority of 1994, airport authorities were responsible for all airport operations and capital projects such as airport expansion, runways, the development of airport lands and airport commercial space. The federal government, acting as landlord, held the leases for a term of sixty years, with an option for a twenty year renewal.

Authorized to set rents for both LAAs and CAAs, Transport Canada looked to the Cabinet documents for the rental framework. The Cabinet documents however represented a maze of conflicting directions resulting in uneven and arbitrary rents for airports across the country. These documents included the eight Guiding Principles in the original 1987 transfer policy, the thirty-six *Supplementary Principles* of 1989, the *National Airports Policy* of 1994, the thirty-six *Fundamental Principles for the Creation and Operation of Canadian Airport Authorities* of 1994, the *Public Accountability Principles* of 1994 and general government directions between 1990 and 1998. Erratic rent-setting resulted from this panoply of conflicting principles. For example, in 1987 LAAs provided for transfer on the basis that the federal government would be left "no worse off"; countering that principle

was one from the thirty-six *Supplementary Principles* of 1989 which required that transfers be based on “fair market value”; countering *that* principle was the one from the 1994 *Fundamental Principles* stating the requirement for “fair value for the federal government with appropriate consideration of the airport’s future earning potential.”

While Canada’s largest and busiest airports were transferred to LAAs and CAAs over that time and while the public interest in air safety was not compromised during the transition, it is questionable whether sufficient heed was paid to the public interest in the equitable disposition of significant public assets (airport assets and business opportunities).

The conflicting priorities in the Cabinet documents provide some insight but fall short of providing a clear and complete picture of the serious issues behind the Canadian airport transfers.

Further shortcomings of the airport transfers were highlighted in the Auditor-General’s Report (2000) and the OECD Report (2001). The OECD found that the public—who should have been apprised fully of issues, such as whether the airport transfer affected its government’s fiscal position, whether the transfer saved money or service delivery or whether the public interest was in any way served—was left in the dark as a result of the lack of initial framework. The OECD Report (2001) claimed that two major factors caused the resulting problems. First, the lack of a valuation of the transferred assets resulted in questionable leasing arrangements and lease re-negotiations. Second, the lack of a defined role for the government as landlord brought about fluid tenancy arrangements and blinkered a public interest requirement.

Lacking an initial framework, Transport Canada created and administered three distinct rent formulas in the first round of negotiations. The Auditor-General found “disturbing” that, with fair market value still not established, Transport Canada would proceed to a second round of negotiations. In the second round, five different formulas were used. Both the O.E.C.D. and Auditor-General Reports found a thorough disregard for the public interest requirements of uniformity, consistency and fairness. The Auditor-General, in providing an example of neglect of the public interest, pointed to the \$185-million rent reduction given to the Greater Toronto Airport Authority (GTAA) to allow for a parallel N-S runway and a de-icing facility and the fact that when the airport was transferred initially to the GTAA, the claim was made then that an important benefit of the transfer would be the provision of a parallel N-S runway and a de-icing facility.<sup>15</sup>

The 2000 Report by the Office of the Auditor-General on Airport Transfers claimed that without any defined policy underpinning the initial airport transfers, ad hoc decision-making was the inescapable consequence. The OECD maintained that the Canadian airports experience “provides an example of the performance problems that occur when a framework of accountability is not established at the outset.”

Policy, which should have preceded change, was established late in the process. The 1994 *National Airports Policy* called for “fundamental change” and based that change on two central facts: first, with 94% of air traffic using 26 of the 726

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airports across the country, the Canadian airport system was overbuilt; second, airports were being subsidized and for the wrong reason.<sup>16</sup>

To meet these concerns, the policy formulated six classifications of Canadian airports, set criteria for each and established the requirements for airport eligibility to the Canadian Airport Authorities. Under the new policy the 26 largest airports were slated to become part of the National Airports system.

The criteria for admission required the airport to be in a provincial capital or service more than 200,000 passengers per year. The federal government would maintain ownership and lease airport management. The second tier of airports included 71 regional or local airports which were to be offered for transfer to their provincial or municipal governments, to local airport authorities or to private entities. By 1999 most of those airports had been divested. The remaining classifications were: small airports, satellite airports, remote airports and Arctic airports. The devolution model of these last classifications—to provincial, local or federal interest—is of less concern to this paper.



### III. Airport Rents and Current Issues

The unfairness of the rent formulas in the airport transfers of 1992-1999 continues to have an effect even today. That effect is reflected in the high landing fees and the resultant inability of Canadian airports to effectively capture air traffic.

To meet the escalating rents set under the rent formulas, Canadian airports resorted to an increase in airline landing fees. During that same time frame, more liberal air agreements were signed which resulted in increased trade, tourism and travel. High landing fees were simply not compatible with increased air traffic. This affected Canadian airports in several ways.

First, airlines tailor or base their routes on competitive criteria and will look to add to their schedules those cities with favourable fee structures, deleting the more expensive ones. Airports with high landing fees are seen as having priced themselves out of the market and can expect reduced traffic. In turn, this can precipitate a downward trend in the importance of an airport, and especially a hub airport.

Economist Dr. Fred Lazar suggests that there is a link between high rents and the diminished role of Toronto Pearson International Airport (Pearson). Before the 2005 rent relief program for Canadian airports, Pearson Airport had the highest landing fees in the world for a Boeing 747, surpassing even Narita Airport near Tokyo, which by that time had reduced its landing fees.<sup>17</sup> Pearson International Airport—a major contributor to the economies of both Ontario and Canada—has witnessed a decline in its status as a hub for several years. In 2001, Airports Council International ranked Pearson as the 26th busiest airport in the world. By 2005, Pearson Airport had dropped to 29th. In its 2008 ranking, both Pearson and Narita Airports had been dropped from the top 30 busiest airports in the world. By 2009, Pearson was ranked 38th.<sup>18</sup> Lazar backs his claim on the decline in Pearson with studies showing the low passenger growth rate of Pearson compared to near-by competing hubs.<sup>19</sup>

## Estimates suggest that nationally there is an annual drain to the U.S. of 5 million Canadian passengers.

Although the decline of Pearson Airport represents a loss to its revenues, a wider and more pressing concern is the overall effect of the decline on the economies of Canada and Ontario. By enhancing connectivity, a hub airport in turn has a positive effect on overall levels of business productivity, 'just-in-time' manufacturing, economies of scale, tourism, market expansion and, ultimately, GDP.

It is estimated that the annual contribution of the Canadian aviation sector is \$33.3-billion or 2.2% of GDP. Passenger loss at Pearson Airport is thus of concern to a wider community than the airport.

Second, more liberal air agreements have resulted in broader travel options, with a growing trend in Internet booking of flights. Often, travel options are based solely on cost with passengers no longer held captive by their home airports.

"It comes down to economics for a family of four flying out of one airport versus another" claims Daniel Robert-Gooch, President of the Canadian Airports Council.<sup>20</sup>

The Surrey Board of Trade reported that, between the Vancouver and Abbotsford Airports, passenger loss to airports across the border at Seattle and Bellingham amounts to one million passengers per year. Estimates suggest that nationally there is an annual drain to the U.S. of 5 million Canadian passengers.<sup>21</sup> The reason for passenger loss, claims the Surrey Board of Trade, is high airport rent. The \$38.8-million airport rent that YVR paid in 2010 makes it uncompetitive with airports around the world.

The issue of declining traffic is even more serious in cargo. Unlike passenger traffic, where passenger loss to U.S. airports is estimated at 20%, cargo routes are tailored entirely to cost and cost-related issues, such as speed of customs clearance. In *Air Competition for Freight*, authors Dr. Michael Tretheway and Robert J. Andriulaitis found that all-cargo carriers tend to have lower operating costs than combination carriers.<sup>22</sup> All-cargo carriers have lower crewing costs, reservation system costs and terminal costs. The authors found that landing fees and airport charges have a "high impact on their (all-cargo carriers) routing choices." Airports compete to offer the best package in order to attract cargo services.<sup>23</sup> Landing fees are a key determinant in those choices.

While the federal government has confined its role in airports to that of landlord, various serious issues have emerged and taken hold over the years.

First, continued government inaction with regard to airport policy is harming the Canadian economy. A series of independent studies by InterVISTAS and RP Erickson & Associates measures the relationship between passenger levels and full-time employment at key airports across the country. These studies provide background and statistics on passenger loss, on employment and the resulting effect on GDP. These studies confirm other studies conducted worldwide on the

strong relationship between privatized airports and economic growth.<sup>24</sup>

Second, airports across Canada have become “workhorses” for the Canadian economy. With limited sources of income and with a continued need to upgrade and expand to attract markets and to meet passenger and cargo demand, Canadian airports are constrained competitively by the enormous rents commanded by the federal government. While increasing landing fees to offset airport rents affects both the airports and the Canadian economy adversely, only the airports must juggle this concern. By contrast, the federal government assumes the role of landlord but without the usual administrative and maintenance commitments incumbent upon a commercial landlord, all the while demanding usurious rents that bear no relationship to the value of the asset and the land.

Third, the rents are inconsistent and unequally applied. The Montreal Economic Institute puts forward the 2005 rents as an example:

“In 2005, Pearson airport paid \$144.4-million in rent, accounting for 27% of its operating expenses, while some airports pay no rent at all. Nearly the full amount comes from the airport administrations in Toronto (48%), Vancouver (27%), Calgary (9%), and Montreal (7%). Even if Pearson is Canada’s busiest airport, its 2004 market share came to only 31% of total traffic. What it pays in rent is thus far out of proportion to the traffic it generates.”<sup>25</sup>

Further, the relationship between rent and revenue at Pearson Airport is not duplicated at other airports. Between 1996 and 2004, Pearson paid \$982.7-million in rent—or 24% of its revenue—while Montreal’s airport rent between 1995 and 2004 was \$83.4-million—or 5% of its revenue.<sup>26</sup> Because of increased claims of usurious rents and their relationship to airport traffic, Transport Minister Lapierre adjusted the airport rent formulas in 2005.

Lazar claims that the ‘new’ rent formula of 2005 resulted in “a vicious circle for airports.”<sup>27</sup> Tying rents to a percentage of revenues required airports to mark up fees by at least the amount of the rent charged. Thus, to net \$100 from a given fee, Pearson—in the 12% bracket—would have to set the fee at \$113.65 (1/1-x where x is the rate for the ground rent).

“So, the 12 per cent bracket ground rate levy results in a mark-up of 13.6 per cent. Under the new formula YYZ’s share of the total ground rents could increase from 48% to 63% by 2010.”<sup>28</sup>

Under the ‘new’ formula, the rent payments in 2011 for Calgary International Airport increased by 40% to \$22.1-million from \$15.9-million the previous year. Projections indicate that Calgary’s rents will increase steadily, “hitting \$33-million in 2014, despite revisions to lease contracts made by Ottawa that lessened the burden.”<sup>29</sup>

The fourteen large airports question the fairness of their funding the system while twelve less busy airports continue to be subsidized by the government.<sup>30</sup> Having called for a new era in airports, the 1994 *National Airport Policy* sought to address questions of over-capacity and to end airport subsidization. Sufficient time has elapsed to assess whether the policy objectives have been met in light of the traffic levels and subsidization of those twelve airports.

“ [T]he Report of the Auditor-General in 2000 found that despite the role of Transport Canada as guarantor of the “integrity and viability” of the National Airports System, it had adopted a “hands-off approach to its landlord responsibilities.”

Based on revenue rather than on land value and, absent any landlord presence or support, the claim is made that the rents are more legally akin to a tax than to a leasehold payment. Barry Rempel, CEO of James Armstrong Richardson (Winnipeg) International Airport, approaches the issue as such.

“By 2020, we will have paid more than \$190-million in rent for an asset that had a book value of less than \$80-million when we took it over. Calling it a rent would indicate we get something back for it, which we don’t. If it’s the government’s desire to use airports as a method of raising additional taxes, then [I] understand their logic. However, if airports are seen as a critical part of a city’s infrastructure and a key cog in economic development, then the government is going about it the wrong way.”<sup>31</sup>

Calgary International Airport CEO, Garth Atkinson notes that with a book value of \$118-million in 1992, Calgary Airport has paid \$332-million in ground rent between 1992 and 2009 alone. Claiming that the high rents are driving up the cost of flying, he seeks a buy out the airport lease by paying the “present value of a future rent stream.”<sup>32</sup>

Finally, transparency and accountability issues affecting airport users and other stakeholders are reduced under the not-for-profit airport model with the privatized model providing the most rigorous standard.

Both the LAAs and the CAAs were incorporated as not-for-profit capital corporations. Transportation economist Tretheway found that by comparison, the CAAs provided “a slightly higher degree of transparency”<sup>33</sup> than the LAAs. To ensure transparency, CAAs publicize price increases in local media, establish a community Consultative Committee required to meet semi-annually to “provide dialogue on matters related to the airport,” establish an annual general public meeting, ensure competitive tender of contracts exceeding \$75,000, and disclose salaries of directors and senior officials.

As landlord, Transport Canada has the right to audit the practices and procedures of the CAAs as they relate to the lease, to the leased premises and to the business affairs of the CAAs. The CAAs are subject to independent review of their management, operation and financial performance every five years.<sup>34</sup>

Yet, the Report of the Auditor-General in 2000 found that despite the role of Transport Canada as guarantor of the “integrity and viability” of the National Airports System, it had adopted a “hands-off approach to its landlord



responsibilities.” The Auditor-General anticipated “significant negative effects in the future” as a consequence. “Areas in need of urgent attention,”<sup>35</sup> were: the increased dependency by airport authorities on airport improvement fees and ownership of subsidiary companies by some airport authorities.

The Auditor-General found that in 1998 airport improvement fees (AIF) had increased to 22% of combined total revenues.<sup>36</sup> Since the creation of the LAAs, Transport Canada had been slow to collect data and to assess the basis of AIF increases. Although Transport Canada had assured decision-makers that the airport improvement fees would be subject to the *Competition Act*, this was subsequently deemed incorrect and competition issues have been left unaddressed.

Further, the Auditor-General revealed that during its five-year review, Transport Canada had collected little information on how airport authorities had used revenues from AIFs. The Auditor-General found that some airport authorities had not yet conducted costing studies to determine the basis of the AIF fee structure and whether the rates were reasonable. The Report outlined some stakeholder concerns “about the use of AIFs, including the quantum of fees that were being charged and the lack of redress mechanisms for the general public.”<sup>37</sup> In early 2012, Vancouver Airport Authority announced an AIF increase of 33%, claiming it was required to offset expansion costs. The announcement was poorly received, with the expectation that there would be further passenger drain.<sup>38</sup> Passenger drain has a direct and quantifiable effect on the Canadian economy and, consequently, oversight of AIF increases remains a pressing federal concern.

The lack of framework for AIF increases in the not-for-profit structure represents a serious deficiency. Current airport users pay for upgrades for the benefit of future users, raising what authors Tretheway and Andriulaitis refer to as “intergenerational issues.”

The Auditor-General expressed further concern over the subsidiary airport ownership of Canadian airport authorities. In her report, the Auditor-General disclosed that at the time of the audit there were “thirteen subsidiaries, most of them wholly owned by the airport authorities created before the LAAs.” These subsidiaries were active in airport management, operational, marketing and consultancy services, including investment in airports in Eastern Europe, South America and South Pacific.

The Auditor-General found that Transport Canada had yet to assess the business and legal arrangements of the subsidiaries and the potential they created for risk to the Crown. The Auditor-General claimed that a relationship with foreign operations could affect airport rents as, with the rent formula structure in place at that time, there could be a downward effect on airport rents should business or intellectual property be transferred off-site. Further, the Auditor-General noted that Transport Canada had yet to assess the financial and political risks of offshore investments by airport authorities, including whether loan guarantees and loan defaults on offshore ventures would affect the viability of the airport authority.

In *Annual Privatization Report 2010: Air Transportation*, author Robert W. Poole, Jr. outlines the subsidiary holdings of the Vancouver Airport Authority:

“Vancouver Airport Services (VAS) announced in June, 2010 that it had acquired a 65% stake in Peels Airports Ltd.’s three British airports—Liverpool John Lennon Airport, Robin Hood Airport Doncaster/Sheffield and Durham Tees Valley Airport. VAS is owned by Vancouver Airport Authority and Citi Infrastructure Investors, and has a global portfolio that now includes 19 airports on three continents.”<sup>39</sup>


To respond to both the concern regarding the lack of framework guiding AIFs and subsidiary holdings by airport authorities, Transport Canada investigated, confirming deficiencies in “the provision of cost data in support of user charges, data on ancillary activities through subsidiaries and the financial interface between LAAs and subsidiaries.”

In response, legislation introduced under Bill C-27 in March, 2003 and again, in June, 2006 under Bill C-20, the *Canada Airports Act* addressed these very issues. The Canadian Airports Council argued against the proposed legislation claiming it would limit operations, negatively impact the activities of airport operations and interfere with subsidiary ownership. In both 2003 and 2006, the legislation did not proceed to passage.

Despite the non-passage of the Bills, these deficiencies remain outstanding. At a minimum, the public interest requires that they be addressed.

In summary, the current airport rent structure under CAAs has provided questionable benefit to airports, to passengers, to cargo and to airlines. Airport rents have an adverse effect on the Canadian economy and on Canada’s competitive position. Attempts to deal with basic oversight in accountability and transparency have failed and remain outstanding.

It may be time to re-visit the *National Airports Policy* of 1994 with a view to adopting a model that will serve the public, the airports and trade more effectively than the current model. Over the years data has accrued on various types of airport ownership, from fully private to partially private under contract services or developer financing. This paper will examine next the privatization of airports in the United Kingdom and the government ownership model of the United States.

 In summary, the current airport rent structure under CAAs has provided questionable benefit to airports, to passengers, to cargo and to airlines.



## IV. Privatization of Airports in the United Kingdom

With the privatization of the British Airport Authorities in 1987, Britain led the world trend toward privatizing airports.

Initially, the Ministry of Defence governed airports in the United Kingdom. In 1965, Britain co-ordinated its airport system, creating a government corporation, the British Airports Authority (BAA) which in 1966 assumed control over Heathrow, Gatwick, Stansted and Prestwick Airports and in 1971 over Edinburgh, Aberdeen and Glasgow airports. In 1987, the Cabinet of The Right Honourable Margaret Thatcher directed the sale of BAA by floating it on the stock exchange in a \$2.5-billion public share offering. Under the *Airports Act* of 1986, BAA (plc) was created as the vehicle with which to raise the funds on the stock market.

By retaining a “golden share” in BAA (plc), the government maintained the authority to veto new airport investment or divestiture. Further regulation under the *Airports Act* of 1986 provided oversight on the allocation of flights to airports, price controls on landing, departure, gate charges and slot sales, and ensured that the concerns of the British economy, airport passengers and the airlines were met. Oversight by the British Competition Commission was put in place to address market dominance and to ensure that competition in the British airport system was neither lessened nor weakened as a result of the transfer.

The fact that 25 years have elapsed since the sale of BAA provides a sufficient time frame within which to assess the privatization model in terms of value, accountability and consumer concerns of price setting and competition.

By 1996, Heathrow was valued at \$4.5-billion, generating profits yearly to its shareholders, including \$455-million in 1995, despite government imposed caps on airline charges and infrastructure improvements of \$782-million (being the rail link connecting Heathrow to central London).<sup>40</sup> In July, 2006, BAA (plc) was taken over by Ferrovial in a \$20-billion bid.<sup>41</sup> The company name was changed from BAA (plc) to BAA. In 2009, Ferrovial sold Gatwick Airport for \$2.47-billion and in October, 2011, sold a 5.88% stake in BAA for £280-million (approximately \$442-million USD).

On issues of accountability, no model can provide greater rigour to the general public than private ownership. Motivated by profit, a private ownership model far surpasses the not-for-profit model. The GAO claimed that greater public

accountability could have been achieved by an unbundled share offering of BAA's seven airports, reasoning that separate sales of the airports would have allowed the government of the UK to maximize its price and to enhance competition.<sup>42</sup>

Regulation under the UK *Airports Act* addressed two price-related concerns: landing fees and congestion. A pricing formula was developed under the *Airports Act* to address the concern that landing fees would increase with privatization. By requiring that airside charges increase by less than the rate of inflation in real inflation-adjusted terms, airside charges decreased steadily. The price-capping of airside fees resulted in a strong incentive to increase revenues on the landside, which resulted in aggressive expansion of airport shopping malls. The pricing structure tackled airside congestion by replacing the traditional base of aircraft weight with a peak/non-peak base. Further pricing structures encouraged a shift to quieter aircraft with noise-related surcharges and rebates.

A review of a recent decision by the British Competition Commission provides insight into the range and resolution of competition issues in a private ownership model. The Competition Commission expressed concern about the 2006 take-over of BAA (plc) by Ferrovial. Given that the take-over involved all seven airports under the BAA (plc), the Commission filed an allegation of market dominance. The Competition Appeal Tribunal investigated the possible adverse effect the take-over would have on passengers and airlines, and required that BAA divest itself of three airports, London-Stansted, Gatwick and either Edinburgh or Glasgow. Having sold Gatwick Airport, BAA proposed to sell Edinburgh Airport. It appealed once more to the Tribunal, claiming a material change in circumstance, based on a forced sale (London-Stansted) in a depressed market and a change in airport markets. BAA claimed that with the pending sale of Edinburgh Airport, it had addressed competition issues, asserting that as the largest airport in Scotland, serving a wealthier catchment area than Glasgow, Edinburgh represented a much larger asset, thus balancing the market. BAA argued further that Edinburgh Airport was not competitive with Glasgow-Prestwick, since they served different markets. Regardless, in February, 2012, the Tribunal rejected the BAA appeal and ordered it to proceed with the sale of Stansted, UK's fourth busiest airport and a short-haul centre. On July 26th, 2012, the Court of Appeal rejected the BAA appeal.

The twin pillars of price-cap and competition oversight in the UK airport model are not without their critics.

The critics claim that although price-capping was to have been temporary, it is still in place at Heathrow, Gatwick and Stansted because the Competition Commission believes those airports retain monopoly power and may charge 'unfair' fees for the use of their facilities. Although new airport construction entails a significant hurdle to entry, it is not insurmountable and, claim the critics, airports are thus not natural monopolies. Further, critics claim that the wide travel options available to the public negate any need for Commission oversight on competition and price issues. To support this position, they point to Heathrow as an example of the strength of existing healthy competition. As a transit airport between continents, Heathrow competes with Amsterdam, Frankfurt and Paris. As an airport serving business and leisure travellers between London and other UK and European destinations, Heathrow competes with Gatwick, London City Airport, rail and road.

Similar findings attach to the other airports.<sup>43</sup>

Critics of price control claim that the limit on airport revenues forces the airports to lease retail stores at the expense of passenger comfort.<sup>44</sup> They also claim that the regulator, the Civil Aviation Authority, does not have a thorough understanding of the capital intensity of airport development and upgrades.<sup>45</sup> To address public concerns of monopolistic practice, critics claim that layers of regulation have stifled airport expansion. As evidence, they point to the veto by the Coalition Government on runway development at key airports and the astonishing eight year approval process<sup>46</sup> required by Heathrow in its application for a fifth terminal, despite evidence that passenger levels had seriously outstripped capacity.

Notwithstanding this criticism, the airport share offering of the seven key UK airports has, on balance, been viewed as a success. With landing fees at Heathrow approximately one-third lower than comparable airports in New York City,<sup>47</sup> the airports in the UK have experienced explosive growth. Private investment has financed expansion and has added important infrastructure, such as the airport rail-link to London.

Transportation analyst, Robert Poole claims that the 1978 de-regulation of the airlines in the US resulted in three 'waves' to airports.<sup>48</sup> The first was the immediate creation of a hub and spoke route system replacing the previous point-to-point system, which was followed by the second wave of low-fare, point-to-point, no-frills service. The third wave was the emergence of the regional jet, allowing for greater access to smaller cities and for increased service to spokes of hubs. Poole suggests that the intensity of the 'waves' was hampered by the failure to de-regulate the airports and the air traffic control system.

It is conceivable that privatizing Canadian airports could spur a similar innovation. A strengthened hub and spoke system, enhanced capacity utilization and re-configured routings at airports are reasonable expectations.

Airline de-regulation in the US in 1978 opened the way for new, no-frills airlines such as Southwest Airlines. Privatizing Canada's airports could result in an increase in essential regional low-fare carriers. In Europe, the proliferation of low-fare carriers attracted investor interest to the smaller, regional airports because they offered attractive and inexpensive alternatives to the congested hubs.

Airport privatization would be a boon to cargo transport. Transportation of cargo by air is on the increase worldwide. Boeing forecasts that by 2018, cargo transport will increase by 6.4% compared to a 4.7% increase for passengers. In testimony before the Standing Senate Committee on Transport, transportation economist Tretheway stressed that cargo will "truck across the border for a difference of one or two cents a pound on any given day."<sup>49</sup> He predicted that, in a more competitive environment, there would be "huge opportunities"<sup>50</sup> for some airports, particularly Winnipeg, Vancouver, Edmonton, Calgary, Prince George and Hamilton—all suited ideally for cargo.

Given the benefits which followed the UK airport system privatization and given the drawbacks of the Canadian not-for-profit model, the UK structure is superior on all fronts and could serve as an exemplar from which Canada could draw with necessary adjustments specific to its requirements.<sup>51</sup>



JFK, NEW YORK, N.Y., U.S.A. (2012)

## IV. Airports in the United States

Airports in the US are owned by a port-authority or by local or state governments. Whereas Canadian airports contribute to government general revenue through rent payments, US airports are subsidized by government. With the high ticket prices in Canada being tied to airport rents, U.S. airports are at an advantage.

Airports in the US are funded from five sources: the Airport Improvement Program (AIP), a tax-exempt bond issue for capital projects, Passenger Facility Charges (PFC), state and local grants, and revenue at the airport such as landing fees, airline leases, parking, etc.

The 2007 US GAO Report estimates that the US airport system receives an average of \$13-billion per year from all sources, of which bonds account for 50%, AIP for 29%, PFC for 17%, airport revenue for 4% and state and local contributions for 4%. The dependence on bonds and AIPs for funding appears tied to airport size with large and medium hubs using bonds and PFCs and relying on AIPs for only 16% and 29% of total capital spending, respectively. By contrast, small hub airports depend on AIP funding for 51% of total spending.

Airports in the US have resisted the worldwide trend towards privatization. US airports continue to be public-sector enterprises exclusively, with devolution to private for-profit corporations not a current consideration. Airport privatization in the US relates only to the possibility of a fixed term lease to private management companies. Prior to 1996, airport privatization or, more accurately, commercialization, in the US was hampered by a combination of "legal barriers, economic constraints and opposition from the airlines and the FAA."<sup>52</sup>

In 2010, authors Poole and Edwards in *Airports and Air Traffic Control*<sup>53</sup> expanded on the impediments:

1. The US state and local airports have for decades received federal aid for airport development and construction. Federal law provides that federal aid for airports would have to be re-paid if the facility were to be privatized.
2. The Federal Airport Improvement Program provides that all airport revenues—including any from a lease or a sale—must be reinvested in the airport from which they originated. A town or city wishing to sell its airport would derive no financial benefit from doing so. Likewise, a buyer would be unable to make a profit since all revenues would have to be returned to the airport. This regulation deters any attempt at selling or leasing.

3. State and local governments can issue tax-exempt bonds to finance airports because they are government owned facilities. Thus, airports may borrow at a lower cost than private airport owners using taxable debt.
4. Concerned that their costs may be higher or they may face increased competition, the airlines have ensured that long term leases at airports have included airline control over concourses and terminals, as well as the right to veto capital spending plans, including airport expansion.

Prompted by the recognition of the significant revenues that commercial airports can generate, the US has renewed its interest in privatization.<sup>54</sup> Emerging evidence confirms that US airports possess “considerable untapped profit potential” which could be managed better by well-capitalized private firms experienced in airport operation.<sup>55</sup> The decline in government funding levels for airports and the budgetary constraints of municipalities coupled with the potential that airports could provide in fiscal relief has made privatization worth a second look.

In 1996, under the *Reauthorization Act*, Title 49, an airport privatization pilot program was launched. The program has been deemed “modest”<sup>56</sup> and as having generated “limited interest, particularly because of slow and rather complex approval procedures and the majority airline consensus rule.”<sup>57</sup>

## The Airport Privatization Pilot Program

1. limited participation to 5 airports; the program required that one be a hub and one be a general aviation airport;
2. provided that participation was to be by long term lease, not sale—except for a general aviation (private plane) airport;
3. allowed the U.S. Secretary of Transportation the right to waive the revenue diversion (“off-airport”) requirement. It was anticipated that this would entice investors by allowing a reasonable rate of return. The U.S. Secretary of Transportation was also given the discretion to exempt a local airport operator or buyer from the requirement to re-pay federal grants and/or reimburse the value of the land;<sup>58</sup>
4. required that the exemptions be approved by both 65% of the airlines serving the airport and by airlines representing 65% of landed weight.

The airports which became part of the pilot program were required to commit to rate increases under the rate of inflation.<sup>59</sup> A higher rate increase required approval by 65% of the airlines serving the airport.

In October, 2006, the City of Chicago applied for the one available slot for a large hub airport and sought to privatize Midway International Airport. The initiative to privatize Midway International Airport had been preceded by Chicago’s lease of parking meters, garages and a long term lease on its toll road, the Chicago Skyway. The Midway International Airport deal provided an upfront exchange of \$2.5-billion in rent for a 99 year airport lease. Investors had hoped that the lease

of Midway International—a major domestic hub—would create a domino effect on airport privatizations but the transfer was not concluded. Reasons for the failure range and have included the \$2.5-billion amount, viewed by some as “eye-popping”; the risk-averse climate of the times; possible issues involving Southwest Airlines and the fact that the potential purchaser was stretched with a recent acquisition in Gatwick International Airport. Although the collapse of the deal inflicted a “huge blow to privatization advocates”, the City of Chicago vowed to revisit the issue, calling the collapse a “little speed bump.”<sup>60</sup>

Hurdles to privatizing US airports include: whether a private airport could survive without government grants and tax-exempt debt financing;<sup>61</sup> issues surrounding property taxes at airports;<sup>62</sup> whether the government is willing to override clauses benefitting certain airlines in current airport agreements;<sup>63</sup> and, the argument over possible foreign ownership in airports in light of the controversial sale of cargo terminals at US seaports to Dubai Ports World of the United Arab Emirates.<sup>64</sup> Substantially, the Midway International Airport privatization project demonstrates the Catch-22 in airport privatization in the US. Robert Kirk claims that privatization by long-term lease could be viewed as “revenue extraction” with the upfront lease payment increasing city coffers without assurance of public funding for future airport upgrades. On the other hand, restricting airport rents to airport purpose provides little incentive to privatize.<sup>65</sup>

A key reason for resistance to privatization in the US is that the major airlines control the airports. Without airline approval (at 65% based on weight and scheduled service), lease payments cannot be diverted off airport. Typically, the airlines have contracted exclusive gate-lease arrangements with the airport which results in airport control. Their contracts give the airlines not only authority over the day-to-day airport operations but also over expansion plans. The airlines are unlikely to consent to any airport expansion plan that would facilitate competing airlines. Privatization does not fit well with the current control of airports by the major airlines.<sup>66</sup>

Only one airport, Stewart International Airport, obtained the approved exemption and proceeded to privatization. Having bought the lease for \$35-million in 2000, National Lease sold it back to the New York and New Jersey Port Authority in 2007 for \$78.5-million. The Congressional Research Service questions the benefit of a privatization that did little more than return the airport to the jurisdiction of the public sector.

“The case can be made that neither the re-purchase of a privatized airport by a public airport authority, nor the quick re-sale at a significant profit of a long-term public lease of an airport built with public funds, was what some supporters had in mind when they supported the privatization project.”<sup>67</sup>

The issue of privatization is complicated further by the poor state of and needed upgrades to the government-owned Air Traffic Control system (ATC). A snapshot of the state of the US air traffic control system appears in the Economist:

“Air travel still relies on a ground-based tracking system from the 1950’s, which forces planes to use inefficient routes in order to stay in contact with



comptrollers. The system's imprecision obliges comptrollers to keep more distance between air traffic, reducing the number of planes that can fly in the available space."<sup>68</sup>

Employee wages and benefits within the ATC in 2010 totalled \$6.5 Billion and represented two-thirds of the operating budget of the FAA. Labour costs, project delays, system obsolescence, political constraints and cost over-runs on major technological advances in ATC have resulted in a crisis in air traffic control.

It is estimated that, by 2020, the cost to the US economy of inaction regarding ATC will be \$40-billion per year.<sup>69</sup> It is entirely possible that the delay in developing air traffic control systems in the US is preventing the privatizing of airports. Conversely, this fact could actually propel government initiatives in airport privatization.

Airports in the US are at a critical stage. US airports have been deemed "mediocre"<sup>70</sup> with high long-term funding needs. The FAA projects that between 2009 and 2013, US airport needs will be \$9.9-billion per year. Airports International projects, over those same years, a need of \$18.9-billion per year. The Congressional Service admits that such high costs provide Congress with interesting challenges, among them a reduction in AIP funding for large hubs and the de-federalization of the larger airports, allowing for an increased reliance on PFCs.<sup>71</sup>

Several secondary issues in airport privatization in the US are worthy of further examination. These issues may affect possible advances on the privatization of airports in the US and include:

- the seniority in airports by the "legacy" airlines and the relationship to the number and location of gate slots at congested airports;
- "residual cost clause" in the lease agreements of the airlines which results in landing fees being tied to airport revenues with landside fee generation restricted as a consequence;
- with approximately one-third of the market carried previously by "legacy" airlines having been eroded by low-cost carriers, the new low-cost carriers are having an effect;
- unpredictable fuel prices;
- economic recession;
- the 2008 House Bill 915 constraining airport privatization.



## V Conclusions

From a Government perspective, the 1992 transfer of airports to not-for-profit corporations provided a great benefit. It allowed the Canadian Government to offset its obligation to operate and finance airports and airport expansion. Further, rather than the government paying for airports and their capital projects, the transfer provided the government with a steady source of income under the airport leases—with the net present value of the leases at \$5.1-billion over 58 years (originally at \$12.9-billion before the rent reduction of 2005). While the federal government continues to reap the benefit, loss has been borne by Canadians, the airports and the Canadian economy.

Because the transfer was to a private, not-for-profit entity, it was assumed that price and other regulatory controls were not required. Yet, subsidiary ownership in two areas remains a pressing concern: (1) the risk issues in the business and legal arrangements affecting the Crown as a result of the subsidiary airports; and (2) the possible effect on airport rents in the event of business or intellectual diversion to subsidiaries.

Equally, the lack of guideline on the use of Airport Improvement Fees raises important issues of accountability. In different ways, the lack of guidance in AIFs affects both airports and airport users.

The airport, lacking recourse to capital investment to finance necessary future upgrades, looks to the flying public through AIF increases for funding. In a privatized model, upgrades would be paid for by shareholder equity levered by debt capital. There would be no higher charges as tomorrow's user would be covering the cost of the newly deployed capital. The current not-for-profit model results in today's airport users funding tomorrow's upgrades. Airport users are awash in taxes, fees and surcharges and a fee to pay for upgrades that will only benefit future users extends the limit of their patience. User intransigence for this type of financing has set in, leaving airports both vulnerable and handicapped.

While charges to airport users are on the increase in Canada, the steady lowering of fees to airport users and airlines in the UK demonstrates the advantage of the privatized model. BAA plc, and its successor BAA, have continuously decreased airport charges including airline and passenger fees since the 1987 UK airport privatization. Legislation accompanying privatization required any increase in charge to be by less than the rate of inflation in real inflation-adjusted terms. Customer satisfaction at Heathrow remains high despite healthy increases in traffic. Since privatization, Heathrow has seen an increase across all areas of air traffic with a 54% increase in passenger traffic, a 34% increase in aircraft movement and a 10% increase in freight. Described as a poster child of privatization, Heathrow has become one of the largest hubs in Europe.

Canadian airports are burdened by major competitive hurdles on pricing with their US counterparts. Unlike Canadian airports, airports in the US pay neither rents nor property taxes. Further, US airports receive government grants for long-term capital projects and are able to finance through the issuance of tax-free bonds. With Canadian airports restricted to raising funds through AIFs and airport revenue, a wide advantage falls to US airports. To remain competitive, airport rent in Canada is a file in need of urgent attention and redress.

Privatized Canadian airports, with pricing and competitive restraints, could answer accountability concerns, provide airports with consistent long-term financing, lower taxes and fees to users and enhance the Canadian economy. Canada has benefited over the years from good airport management and oversight. The present value of airports provides the Canadian government with a wide horizon of possibility. The British airport structure allows a good base model which could be adapted to meet the particular needs of Canadian airports.

# Endnotes

1. J.R.K. Main, *Voyageurs of the Air* (Ottawa: Queen's Printer, 1968), p.28. ←
2. *Air Administration in Canada in 1919* (Public Archives Canada, RG 24 DOC 3564 1011-1-15). ←
3. Ibid. ←
4. These airports were the seaplane bases at Vancouver (Jericho Beach) and Roberval along with airports at Ottawa (Rockcliffe) and Morley in Alberta. ←
5. The Comptroller of Civil Aviation claimed in a March 17, 1933 letter to the Deputy-Minister of Defence that although U.S. operators were "ambitious to extend their operations and increase their traffic", the decision to survey and build the Trans-Canada Airway had "effectively blocked this penetration for the time being". ←
6. Radio Broadcast by the Honourable D.M. Sutherland, Minister of National Defence, (March, 1934); Appendix 25, *History of Canadian Airports*, by T.M. McGrath. ←
7. Boswell, Randy, "From birth to life-support in exactly 64 years", *Ottawa Citizen* (April 3, 2003). ←
8. A notorious cigar smoker, the federal Minister of Transport often joined the flight and would get out at the many stops along the way to "meet & greet" and have a smoke. He had apparently been told he could not smoke on the plane. See "From birth to life-support in exactly 64 years", *Ottawa Citizen* (April 3, 2003). ←
9. Office of the Auditor-General of Canada, (2000) *Airport Transfers: National Airports System* at 10-20. ←
10. By contrast, prior to WWII, airports in the US were a local responsibility. After the war, the 1946 *Federal Airport Act* continued aid but at lower levels than during the war years. ←
11. For example, McGrath notes that Manitoba offered grants and loans whereas Alberta offered 100% capital cost assistance. Ontario offered capital assistance of up to 80% and operating assistance of 50%. ←
12. In order to maintain an airport at Lethbridge as well as one at Grande Pointe, Alberta funded capital upgrades. By agreement with Transport Canada, Alberta's financial commitment would be repaid and the airport transferred to Transport Canada. ←
13. *Proceedings of the Standing Senate Committee on Transport and Communications*, Evidence of March 2nd, 2011. ←
14. In 1985, debt represented 44.6% of GDP. The Library of Parliament claims that further reasons for commercialization of government assets include its potential to increase private-sector competition which could boost the economy; reduced demand on decision-making apparatus of government; cash flow. ←
15. Office of the Auditor General at 10-102. Examples of inconsistent treatment of other airports include Calgary Airport which had a ceiling on its rent along with the Transport Canada agreement of future passenger numbers below the then current level. Edmonton Airport lease provided that Transport Canada would pay negative rent to fund shortfalls in airport revenues. ←
16. *National Airport Policy* noted that in 1994, \$2.3-billion in direct & indirect subsidies underpinned transportation and infrastructure. ←
17. *Montreal Economic Institute Economic Note* of November, 2006. ←
18. Airports Council International Rankings. ←
19. *The potential economic impacts of reducing the federal government's ground rents for Toronto Pearson International Airport and reducing the Federal Excise tax on aviation fuel*: Dr. Fred Lazar (Feb. 6, 2007). ←
20. Carman, Tara, "High travel levies hurt Canadian airports" (*Vancouver Sun*, November 11, 2011). ←
21. The Hotel Association of Canada reported that in 2010, 21% of Canadian leisure travellers had travelled to a U.S. airport by car with a further 11% "looking at that option". ←
22. Combination carriers (as opposed to all-cargo carriers) are passenger aircraft that carry passengers on the main deck and provide cargo capacity in the bellyhold. Cargo rates for combination carriers are marginally-priced. ←
23. As an example, Tretheway & Andriulaitis cite the routing change of Ethiopian Airlines from Brussels to Liège based on cost, specialized handling services and speed of customs clearance. ←

24. The InterVISTAS' studies also measure the economic impact of rent reduction at airports. Dr. Lazar's paper, referenced in footnote 24, reviews these studies and the economic impact studies on airports globally. ←
25. *Montreal Economic Institute, Economic Note*, November, 2006 at p. 2. ←
26. Severs, Laura, "Aviation industry seeks rent reduction", *Business Edge News Magazine* at p. 1. ←
27. Lazar, Fred: *The Potential Economic Impacts of reducing the Federal Government's ground Rents for Toronto Pearson International Airport and Reducing the Federal Excise Tax on Aviation Fuel* (February 6, 2007). ←
28. *Ibid*, at p. 9. ←
29. Jang, Brent, "Calgary airport, Ottawa at odds over lease costs", *Globe and Mail*, September 6th, 2010. ←
30. Brooks & Prentice, *Airport Devolution: The Canadian Experience*. The authors compare airport policy to clubs, such as golf clubs where, the greater the number of members, the greater the intended benefit for all. ←
31. Kirbyson, Geoff, "Airports call on feds to reduce their rents", *Winnipeg Free Press* (January 28, 2005). The reasoning of Barry Rempel parallels that of the Montreal Economic Institute. They claim the book value of the total Canadian airport infrastructure transferred since 1992 is \$1.5-billion. By contrast, rents paid between 1996 and 2006 by the NAS airports have been \$2-billion. ←
32. *Supra*, footnote 29. ←
33. Tretheway, Michael and Andriulaitis: *Airport Policy in Canada: Limitations of the not-for-profit governance model* (Brookings Institute, 2009). ←
34. *Ibid*, at page 141. ←
35. Auditor-General Report (2000): *Airport Transfers: National Airports System* at 10-108 and 10-110. ←
36. In 1998, Airport Improvement fees amounted to \$116-million. ←
37. Auditor-General's Report at 10-114. ←
38. Hume, Mark, "Fee hike overshadows airport expansion plans", *Globe and Mail* (January 29th, 2012). ←
39. Poole, Robert W., *Annual Privatization Report 2010: Air Transportation* at page 7. Recent reports indicate an anticipated bid by Vancouver Airport Authority for Edinburgh Airport. In a January, 2008 joint submission by the airports of Vancouver, Toronto and Montreal, the suggestion was advanced that profits from overseas subsidiary ownership "would flow to the not-for-profit CAAs to fund capital and operations thereby reducing fees charged to Canadians and making CAAs more competitive. ←
40. GAO Testimony (1996) *Airport Privatization: Issues related to sale or lease of U.S. commercial airports* at p. 5. ←
41. *Airwise* (January 5th, 2012) and *Reuters* February 1st, 2012 claim the take-over bid to be £10.3 or \$16-billion USD; the *Economist* (July 5th, 2007) values the sale at £10-billion (or \$20-million USD). ←
42. *Supra*, footnote 40 at page 6. The Australian airport privatisation involved sale by competitive bid with the short-listing of bidders resulting in ownership divided between ten private sector consortia. ←
43. Scott, Peter: *Economic Regulation of Airports in the U.K.*, University of Bath, School of Management. ←
44. "Britain's Awful Airports", *The Economist* (August 9th, 2007), quoting London Mayor Ken Livingstone that Heathrow keeps passengers "as prisoner" in "its ghastly shopping mall." ←
45. Citing the re-adjustment of the cap on BAA's rate of return despite efficiency gains, Reddy, Karthik: *Airport Regulation in the United Kingdom*, November 17th, 2010 quotes Peter Scott of The University of Bath School of Management that the maximum price set by the regulator as "not the result of some clear economic rule but of informed judgment in the midst of great uncertainty." ←
46. The Heathrow T5 regulatory hearing is the longest planning inquiry in the history of the U.K., per Keith Boyfield, David Starkie, Tom Bass & Barry Humphreys, "A Market in Airport Slots", *Institute of Economic Affairs* (2003). ←
47. "The man who bought trouble", *The Economist* (July 5th, 2007). ←
48. Poole, Robert W., Jr. & Edwards, Chris: *Airline deregulation: The unfinished revolution* (2010). ←
49. Proceedings of the Standing Senate Committee on Transport (March 2, 2011) at page 3. ←
50. *Ibid*. ←

51. For example, the 99 year lease of 17 of the 22 Australian airports, which took place in two phases in 1997 & 1998, provides an interesting variant to the UK privatisation model. In 2002, Sydney International was leased under a similar arrangement for \$3-billion. ←
52. GAO, Testimony before the Subcommittee on Aviation, Committee on Transportation & Infrastructure (1996) at p.6. ←
53. Poole, Robert W. and Edwards, Chris: *Airports and Air Traffic Control, Downsizing the federal government* at p.4. ←
54. "Airports like LAX are tremendous assets. But the city has never gotten a penny back on its investment." claimed the director of LA Department of Airports on the proposed sale or lease of the city of L.A.'s 4 airports in *Los Angeles Times*, "Sale, leasing of Airports under study" (January 14th, 1991). ←
55. In 1995, BAA won a 10 year management contract for the Indianapolis Airport with fees based on the savings it could generate rather than the usual fixed management fee. ←
56. Ibid, footnote 51. ←
57. Graham, Anne: *The regulation of US airports*, November 9, 2002 workshop at p. 6. ←
58. Previous Court challenges had (1) disallowed pricing directed at reducing congestion at Boston's Logan Airport (PACE case) and (2) disallowed the taxing authority of Los Angeles on its airport, LAX. Both cases confirmed that local governments may not siphon off airport revenues for non-airport purposes. ←
59. In Aviation privatization makes headway: Aviation Week, June 18th, 2010, Poole claims that this form of costing would be airline approved for reasons of pricing predictability. ←
60. Huff Post Chicago, "Midway Airport privatization deal collapses" (February 4th, 2012). Having obtained the requisite 65% airline approval, the lease agreement "set the pace, process and expectations" for future airport deals claimed anchor tenant, Southwest Airlines. ←
61. Privatised airports could still participate in the AIP but at the lower federal rate of 70%. In *Airports and Air Traffic Control*, Robert Poole Jr. claims that the hurdle of bond financing could be overcome by tax reform reducing or eliminating the tax exemption on bonds. Alternatively, the government could allow private operators to make use of these bonds ('private activity bonds') as it had for toll road operators. ←
62. *City of L.A. vs. U.S. Dept. of Transp.*, 165 F 3d 972 (D.C. Cir. 1999) Opportunity cost vs. historic cost in land valuation was reviewed including the effect on landing fees. Opportunity cost base resulted in tripling of landing fees and ground LAX to a halt. ←
63. Graham, Anne: *The Regulation of U.S. Airports: Recent Developments in Australia, North America and Europe*, November, 2002 at page 6. The author looks to the proposed 1995 sale of John Wayne Airport to off-set the bankruptcy of Orange County. The sale was not pursued due to the likelihood of litigation by the airlines on grounds of the unlawful use of revenues for non-airport purpose. This, claims the author, demonstrates the strength of the airlines. A more recent example was the planned slot auction by the FAA to relieve congestion at three New York Airports. Opposed by the airlines, the Bush administration was forced to abandon the proposal. ←
64. New Interest in US Airport Privatization: Jacobs Consultancy (May, 2007). ←
65. Kirk, Robert S.: *Airport Improvement Program(AIP): Reauthorization Issues for Congress* (May 29, 2009). ←
66. In 2010, Poole noted that "only one airport has been privatized over the last decade." The 2010 *Annual Privatization Report* by the Reason Foundation records no new applicants for the hub airport slot in the pilot program. ←
67. Supra, footnote 63 at p. 32. ←
68. Life in the slow lane: *The Economist* (April 28th, 2011). ←
69. Supra, footnote 60 at p. 5. ←
70. Supra, footnote 66. ←
71. Poole, Robert, "Remove the Airport Poison Pill", *Airport Policy & Newsletter* #64. ←

Further Reading



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## Canada's Not-So Friendly Skies

By Mark Milke

<http://www.fcpp.org/publication.php/3335>



November 2009

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By Adrian Vannahme

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