



CAC Response to Transport Canada
Canada-United States Air Transport Agreement
Consultation with Stakeholders Document

June 30, 2005

Canada-U.S. Air Transport Agreement

1. Should the Government of Canada enter into negotiations with the U.S.A. to further liberalize the 1995 Agreement?

Yes. The Canadian Airports Council (CAC) supports further liberalizing the Canada-U.S. Agreement. It is universally accepted that the 1995 agreement has provided significant economic benefits for both countries. The question is not should we proceed, but rather how quickly do we proceed and what are the next steps.

Caution needs to be placed on how the questions have been individualized. It is imperative that it is recognized that positions on the questions are not exclusive from one another. For example support for fifths and yet undermining cargo co-terminalization will likely fail to further liberalize the agreement.

It is our view that we take a 2-phased approach as part of one continuous set of negotiations.

1. This year we move to implement a basic open skies agreement that would include open fifths for pax and cargo, cargo co-terminalization and 7th freedoms for cargo. The standard U.S. Open Skies model.
2. Immediately thereafter continue discussions that will encompass the more contentious and complicated issues such as Right of Establishment, and a "Common North American Aviation Market". The outcome of this phase to be negotiated and implemented by the end of this decade.

Traffic rights cannot be seen in isolation. There is little value in securing such rights if they are not useable because of facilitation or security impediments. In phase 2 for example, if we pursue a "Common North American Aviation Market" this may need to go in parallel with a Perimeter Clearance initiative

Fifths

2. Should Canada negotiate unrestricted (i.e., capacity and points served) fifth freedom rights for scheduled passenger and all-cargo services with the U.S.A.?

Yes. We see open and unrestricted fifth freedom rights for passenger and cargo services as being an integral part of a true Open Skies agreement with the U.S.

3. What are the benefits/risks of a regime of unrestricted fifth freedom rights?

The benefits can be sizeable.

- It will be a facilitator of trade and tourism
- It will provide consumers – the public and the cargo end user greater choice
- New international services for medium sized communities; by having the U.S. and Canadian points providing the necessary market support
- A U.S. carrier operating a direct service from a market such as Salt Lake City or Kansas City to Winnipeg to London, or additional competitive services, i.e., YHZ to Europe by a U.S. carrier. Similarly a Canadian carrier could access South Africa or secondary points in Latin America via a U.S. point.

On the cargo side, 5ths for cargo will provide U.S. and Canadian all-cargo and integrate greater choice and access when operating international services. Canadian exporters and businesses would have the potential to realize significant benefits. Greater wide body capacity on the transborder sector resulting from 5ths for passengers would also generate additional transborder air cargo capacity. Currently transborder passenger combination capacity is almost exclusively narrow body, thereby limiting the carriage of cargo.

When looking from a broader perspective, risks are minimal. These would be limited to how and if the carriers wish to exercise such rights.

4. Would Canadian and/or U.S. air carriers exercise fifth freedom rights beyond each other's markets? What are likely destinations for passenger and all-cargo services?

Significant potential benefits exist for large and medium sized Canadian communities. Fifthths could support the introduction or expansion of international services from medium sized communities and support larger communities to introducing services to secondary international destinations. This will give airlines increased options and flexibility.

Sevenths for Cargo

5. Should Canada negotiate unrestricted seventh freedom rights for all-cargo services with the U.S.A.? If so, what are the anticipated results?

Yes. We support sevenths for cargo as a key ingredient of an Open Skies agreement. We see such rights as being of benefit to Canadian carrier interests. Opportunity for U.S. carriers exercising such rights appears to be limited as they would more likely utilize fifthths.

6. Alternatively, should Canada negotiate a more limited exchange of seventh freedom all-cargo rights? If so, which ones and why

Preference should be to negotiate unlimited sevenths, however as a fallback position on a more limited exchange could still be beneficial.

7. Would Canadian/U.S. airlines exercise all-cargo seventh freedom rights beyond Canada and the U.S.A.? What are likely destinations?

Destinations for U.S. carriers excluding Canada would be limited; rather we see these carriers intentionally using fifths. On the other hand we see greater opportunities for Canadian carriers to exercise sevenths. It is however premature to determine destinations to be served as this would be subject to the nature of the Canadian cargo carrier industry – fleet, strategy, alliance, etc.

8. Should seventh freedom rights for passenger services be negotiated?

This should be considered as part future discussions of a Common North American Aviation Market.

Pricing

9. Should the ability for U.S. airlines to be price leaders in Canada-third country markets (operated via a connection in the U.S.A.) and for Canadian airlines to be price leaders in U.S.-third country markets (operated via a connection in Canada) be guaranteed?

Yes – let market forces and carrier pricing strategy dictate pricing levels whether it be 3rds/4ths, 5ths or 6ths. In reality carriers operating sixth freedom markets have a competitive disadvantage over 3rd/4th carriers serving the same markets. It is accordingly natural that pricing on sixth freedom services would typically be less than 3rd/4th freedom sectors.

Flight Numbering

10. Should Canada allow a single flight number to be used for a Canadian air carrier offering U.S.-third country service (operated via a connection in Canada) or for a U.S. air carrier offering a Canada-third country service (operated via a connection in the U.S.A)?

Yes, we fully support through flight numbering. It will provide increased customer convenience.

Cargo Co-Terminalization

11. Should Canada lift the prohibition on all-cargo courier co-terminalization? If so, what would be the anticipated results? Can you quantify these results?

Although there could be some limited negative impact on Canadian all-cargo carriers, a number of stakeholders would benefit from the removal of the prohibition against co-terminalization. Major beneficiaries include:

Shippers:

- Eliminating the time required to transfer goods between Canadian and U.S. aircraft, or for trucking goods to gateway airports to load on U.S. aircraft, could provide shippers with later cut-off times. This would allow more of the day's production to be shipped on an overnight delivery basis and later cut off times for new orders, features particularly important for distribution-related activities, activities that inland points have more difficulty supporting than gateway communities.
- In a similar manner, eliminating the time required to transfer goods between U.S. and Canadian aircraft, or for transferring to truck to ship goods from gateway airports to inland points means earlier delivery times of goods, parts and parcels needed by Canadian businesses and consumers.
- The U.S. integrated carriers typically use larger aircraft than the Canadian carriers they currently contract out service to. The use of larger aircraft gives shippers greater flexibility in what and how they ship cargo.
- Efficiency gains through co-terminalization could lower costs, and could potentially lead to lower rates to shippers, or at least more stable pricing.

Communities:

- Communities could potentially attract distribution type activity that current early cut-off shipping times make difficult to support.
- In some cases, a switch to U.S. integrator aircraft could result in lower noise impacts, as these carriers have undertaken programs to lower noise emissions, particularly important given the occurrence of most of the operations at night.

Airports:

- The use of larger aircraft will lead to increased airport revenues through increased landing fees.
- U.S. integrator services being extended to a greater number of Canadian communities could lead to additional investment in facilities by the integrated carriers.
- There may be a transfer of some handling fees, parking fees, and employment among airports, particularly from the large gateways to smaller and interior points.

- 12. Do you believe that Canadian/U.S. all-cargo courier carriers would take advantage of the removal of the co-terminalization prohibition? If so, can you identify specific city-pairs where co-terminalization is more likely to be exercised by U.S. or Canadian carriers?**

See answer above.

Charter

- 13. In a scenario where scheduled rights are unrestricted, is there a need to have a regulatory distinction between charter and scheduled services?**

No, there is no need to have a regulatory distinction between scheduled and charter services on the transborder market. For all intents and purposes it does not exist today.

- 14. What are the implications for Canada of liberalizing charter operations for U.S. air carriers in Canada-third country markets? Are there benefits for Canadian air carriers in U.S.-third country markets? If so, what are they?**

The Canada-U.S. Agreement minimally differentiates scheduled from charter. Accordingly it appears to be logical to permit "Charter" carriers. This would provide network support to those carriers and provide consumers greater choice. Benefits for Canadian carriers would allow Canadian charter carriers to combine their U.S. with International services. We would also be supportive of through flight numbering for these carriers. Specific benefits for example could include connecting Florida flights with European.

- 15. Should Canada agree to give the choice to Canadian and U.S. air carriers to operate under the charter regulations of either country in the Canada-U.S., Canada-third country, and U.S.-third country markets? What would be the advantages of such an initiative?**

Charter carriers should have to follow the same rules as scheduled carriers.

- 16. Does a potential reduction in Canada's economic oversight of Canadian originating charters operated by U.S. and Canadian carriers pose a problem for stakeholders?**

In principle, no.

Wet Leasing

17. In the absence of the restrictions described above, would there be opportunities for Canadian air carriers to wet lease to U.S. air carriers for domestic U.S. or U.S.-international air services?

Yes, however it will be up to the carriers to take advantage of the new opportunities.

Code-Sharing

18. Should Canada accept the U.S. "Open Skies" approach to code-sharing? What would be the anticipated results?

Code-sharing will benefit American carriers the most. This is an area that Canada may be able to use as possible leverage during negotiations.

Facilitation

19. In the context of a further liberalization of the Agreement, which aspects of facilitation do you believe are the most important?

Traffic rights cannot be seen in isolation. There is little value in securing such rights if they are not useable because of facilitation or security impediments. A number of facilitation issues such as:

- staffing and hours of operation of the pre-clearance facility
- connecting bag impediments
- transfer departure facilities
- international transfer departure facilities; and
- the Nexus program.

It may be best for Canada to table and acknowledge such issues, and rather than attempt to directly try to resolve such issues as a precondition for liberalizing the agreement, receive a commitment that we will work in parallel to resolve the impediments. This could be undertaken in a manner similar to the 1995 agreement where there was a commitment to resolve some facilitation and regulatory issues (i.e. In-transit Pre-clearance).

Fly America Act

20. Have the constraints imposed by the Fly America Act had a material effect on Canadian air carriers? If so, what are they?

We are not aware of any significant impact on Canadian carriers.

21. Should Canada seek to have restrictions imposed by the Fly America Act removed?

The CAC suggests that this be dealt with only under the auspices of negotiating a Common North American Aviation Market.

Other

22. Are there any other issues/additional items that you would like to raise that pertain to the potential liberalization of the Agreement?

- As stated in the preamble in Question 1
"Caution needs to be placed on the how the questions have been individualized. It is imperative that it is recognized that positions on the questions are not exclusive from one another. For example support for fifths and yet undermining cargo co-terminalization will likely fail further liberalize the agreement. It is our view that we that a 2-phased approach."

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Immediately thereafter continue discussions that will encompass the more contentious and complicated issues such as Right of Establishment, and a "Common North American Aviation Market".

- When developing a mandate, take into account (place greater weight than it has in the past) all stakeholders and especially the communities, and user groups. This is not predominantly an air carrier issue.
- Individual airports, on behalf of their communities and regions, must have the opportunity to actively participate in these negotiations. The CAC position is that the CAC and its members that wish to participate in bi-lateral negotiations "must" be accorded "Observer Status" comparable to Canadian air carriers and actually comparable to airports in the U.S.
- Another area, CAC wishes to bring to the attention of the Government of Canada is the U.S. anti-trust immunity. We estimate that in order to enhance its role and increase commercial opportunities in the Star Alliance, Air Canada must obtain anti-trust immunity on the North Atlantic sector from the U.S. Government. On the other hand, the U.S. authorities will not grant such right unless both countries have signed the U.S. model Open Skies Agreement. Consequently, we recommend that such a key item be given the necessary attention during the upcoming negotiations.

Long Term (assumes 2007-2010 time period)

23. Is an integration of the Canadian and U.S. air transportation markets in Canada's overall transportation interests?

Yes – the move to global liberalization in hand with the Canada-U.S. NAFTA agreement is moving our two countries closer in our trade relationship. Canada and the U.S. have experienced integration in most other industries and yet, perhaps the result of precedent and inertia, air transportation has been treated as a unique case. The integration of the Canada-U.S. air transportation system will bring efficiencies to the air carrier industry, would parallel the NAFTA agreement and our growing trade relationship. It would also potentially parallel other initiations such as perimeter clearance.

24. Should Canada be prepared to allow U.S. air carriers (operating under U.S. rules) to serve the domestic Canadian market and vice-versa? What would be the anticipated results?

Cabotage

This issue needs to be considered, however further study is required.

25. Should U.S. entities be allowed to establish or acquire an air carrier in Canada, making it entirely U.S. owned and controlled but certified and licensed in Canada and compelled to operate under the same rules as Canadian carriers (right of establishment)? What would be the anticipated results?

Yes, this seems to be a natural step in evolving the Canada-U.S. agreement
Benefits would include:

- access for foreign carriers to beyond gateway markets that are currently limited. In Canada we in effect have a monopoly situation with respect to allowing access by foreign non-Star international airlines to secondary or beyond the gateway communities. We have only one all service carrier that has a suitable domestic network.
- added capacity and choice for smaller secondary communities
- addressing the shortage of investment capital, especially in Canada

One such highly successful example includes Virgin Blue in Australia.

It is our understanding that U.S. carriers (at least one regional airline) are interested in this concept. It would provide Canadian carriers or entities greater access into the U.S. markets.

26. If rights of establishment did become possible, should they apply to air carriers operating domestic air services exclusively or to air carriers operating domestic and international air services?

We see the concept as applying exclusively to domestic with the focus not being on the long transcon services but rather to provide a competitive situation to the regional markets.

When we pursue the Common North American model, this by definition would be expanded into transborder and international markets.

Organizations such as the European Union and ICAO are now proposing that domestic ownership and control requirements be replaced by the carrier's primary place of business as the determining factor. If Canada pursues such a policy with the U.S. and other countries, it would facilitate the concept of right of establishment both domestically and internationally.

27. From your perspective, what are some of the other key issues pertaining to the further integration of the Canadian and U.S. air transportation markets?

We would recommend focus and co-ordination be placed on facilitating the movement of passengers across the border.

- Common plan or understanding among internal Canadian government departments and agencies to achieve overall national goals.
- Perimeter Clearance
- Improved pre-clearance staffing and hours of operation.