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| Airport privatization:Killing the goose that continues to lay golden eggs |

A research paper by

The Union of Canadian Transportation Employees



Airport Privatization:

Killing the Canadian Goose that Continues to Lay Golden Eggs

# Introduction

Canada’s airports are amongst the best in the world. They pay their own way by using a user-pay system that passes the costs directly to air travellers. They make massive investments in local communities such as a $300 million-dollar contribution towards new SkyTrain stations in Vancouver. They build shopping centres right on their property that not only generate additional economic activity, but win awards for design and efficiency. They work great just as they are.

Why then is the Federal Government talking about privatizing them again? We do not understand it, and we are not alone. In 2008, the International Air Transport Association said in a briefing on airport privatization:

*“Commercialization has resulted in significant increases in the airport and ANC cost-base that are used to determine charges... In addition, the promised increases in efficiency and productivity have not always materialized.”*

Closer to home, Mr. Mark Laroche, President and Chief Executive Officer of the Ottawa International Airport Authority and Craig Richmond, President and Chief Executive Officer of the Vancouver Airport Authority wrote in the Globe & Mail that:

*“Canada is now recognized as having the best aviation infrastructure and most efficiently run airports in the world and winning awards in design, innovation, safety and customer service. And, under the current model, we do it without government funding. In fact, our airports contribute more than $1-billion a year in rent and other fees to the government.”*

The truth is that we are talking about selling off Canada’s airport assets because some politicians want to take our public assets to finance their political promises. And some people in the private sector think they can make more money from the travelling public. In 2014 the C.D. Howe Institute stated:

*“Airport authorities make long-term commitments that the looming end of leases may soon jeopardize. The federal government should sell its remaining interest in the leases either to the not-for­ profit airport authorities that operate them or to for-profit corporations. Such sales could make investors, airlines, travelers, and taxpayers all better off.”*

Benjamin Dachis, C.D. Howe Institute, Full Throttle: Reforming Canada’s Aviation Policy, January 2014.

The problem is that everyone but investors and shareholders would have no guarantees of being better off, and most experts agree that there are definite risks in this process. They include the facts that costs to travel by air will increase, passenger experience will deteriorate, we will lose community control of our airports, and the Canadian government will have to swallow all existing debts on our airports to make it attractive to potential buyers.

The bottom line on privatizing Canada’s airports is that it does not make sense. Unless you are an investor who wants to cash in. Or a cash-strapped government that wants to get a cash infusion by selling off our public assets. It would be in effect long-term pain for a very short-term gain. The real question for Canadians should be: Why are we willing to sell off a goose that continues to lay golden eggs that we all benefit from?

# Current Status

So how did we get here? On June 25, 2014, the federal Minister of Transport launched a review of the *Canada Transportation Act*. Chaired by David Emerson, the committee presented *Pathways: Connecting Canada’s Transportation System to the World* (aka the Emerson Report) to the Minister of Transport in February 2016. It contained a number of recommendations about all modes of federally regulated transportation in Canada. In particular, it made a number of specific recommendations that related to the further privatization of Canadian airports. We will review the options suggested by the Emerson Report later in this document.

Since the federal government has received the report Canadians have heard very little until recently. In October 2016, it became public that the federal government have asked one of the world’s top investment banks to determine how much of an economic windfall Ottawa could reap by privatizing Canadian airports. The government, through a Crown agency responsible for selling off federal assets, has hired Credit Suisse AG to analyze several privatization options before the end of the year.

According to the Globe and Mail, this contract with Credit Suisse AG will provide Finance Minister Bill Morneau with a range of options to consider as he prepares his 2017 budget – though his office insists no decisions are imminent. Canada’s top eight airports – Toronto, Vancouver, Montreal, Calgary, Edmonton, Ottawa, Winnipeg and Halifax – will be reviewed individually, including with on-site visits.

# History of Airport Privatization in Canada

In the 1980s, the federal government ended its direct ownership and operation of Canada’s airports. It adopted a system in which the federal government retained ownership of the land, but transferred the operation of the largest 22 federally owned airports to airport authorities that run on a not-for-profit basis and pay rent to Ottawa.

Most airports were fully divested. Only 18 small airports remain under the direct ownership and operation of the federal government. Ottawa currently receives about $1-billion a year from airports in rent and security fees. The airport authorities are responsible for covering the cost of infrastructure maintenance and upgrades through passenger fees.

An excerpt from the Emerson Report on this history reads:

*Thirty years ago, Transport Canada owned and operated most airports across the country, as well as the air navigation system. Most of the infrastructure was built to the highest architectural and technological standards in the 1950s and 1960s, but by the mid-1980s, the system was aging and approaching the end of its useful life. Competing priorities for public funds and government debt levels were pushing the government-operated model to a breaking point. Federal budgets would not bear the replacement cost of the airport and air navigation systems, which were increasingly ill-suited to growing traffic and new security requirements as a result of violent attacks targeting air transport.*

*Following a series of studies in the 1980s, and the privatization of airports in the United Kingdom, Canada commercialized air navigation services (Nav Canada) and the larger airports, and adopted the user pay approach to building and operating air infrastructure across the sector. Beginning with Vancouver, Calgary, Montréal and Edmonton, from 1992 to 2003, the operation of the largest 22 federally-owned airports (those with traffic levels above 200,000 passengers per year and/or located in provincial capitals) were transferred to 21 airport authorities.*

These not-for-profit, non-share capital corporations were created with a mandate to develop and operate the airport and lands safely, securely, and for the economic development of their regions. Most are incorporated federally under the *Canada Not-for-profit Corporations Act*, but some (including Calgary and Edmonton), are incorporated under provincial legislation. The Crown retained ownership of the lands and assets, under relationships governed by 60-year leases (with one 20-year renewal option). The authorities pay rent, and at the end of the lease, they must turn over a world-class airport, with no debt to the government. As the end of lease approaches, authorities will have increasing difficulty borrowing to maintain/improve assets, and leasing to businesses operating on airport lands. Airport authorities are free to set fees, take on debt, and operate subsidiaries.

The National Airports Policy created the National Airports System, which included the 22 airports operated by airport authorities, along with the airports in the two territorial capitals – Whitehorse and Yellowknife – which were transferred to the territorial governments, and Kelowna, which is operated and partly-owned by the municipality. Iqaluit was added to the National Airports System upon the creation of Nunavut. These four airports, are not subject to the same lease and rent requirements.

# Why the Canadian Airport System Works

The Canadian system is the model of the world. One that almost everyone else looks up to. Here’s what a world-renowned expert in airports has to say:

*The Canadian system is the only one based on non-for-profit corporations.*

*Canadian Airport Authorities (CAA’s) are non-share capital corporations incorporated under Part II Canada Corporations Act.*

*CAAs do not pay dividends but pay rent to the Government of Canada as well as municipal taxes.*

*All “profits” are reinvested.*

*Main sources of funds are cash flow from operations, airport improvement fees (AIFs) and debt instruments – Government grants for infrastructure are exceptional.*

Pierre Gagnon,

Vice-President Legal Affairs and Secretary,

 Aéroports de Montréal.

Mr. Gagnon goes on to say that the Canadian model actually works well. He adds that major Canadian airports rank among the best, they are efficient and infrastructures are well maintained and regularly upgraded. Most airports are 100% common-use for improved utilization. Financing is simple and expansion projects are tied to community needs, not government agenda. He concluded by saying that community involvement is a “plus.”

In a presentation to the Transportation Review panel in April, 2015 the Aéroports de Montréal went even further in their praise of the Canadian model. An extract from that submission reads:

*It is an undeniable fact that the Canadian model has allowed to achieve the prime objective of the government, i.e. the reduction of the administrative and financial burden related to the management, operation and development of the national airport network. At the same time, the Canadian model has enabled the establishment of a network of efficient airports, distributed across the vast Canadian territory. According to the World Economic Forum, Canadian airports rank first in the world for infrastructure quality. Across Canada, the capacity of the airports has followed the increase in traffic.*

On the whole, the major Canadian airports are designed to deal with three types of traffic— domestic, cross-border and international—in a safe and efficient manner, and the shared use of the airport facilities by the various airlines translates into efficiency gains and cost savings. They are also at the forefront in using advanced technologies to simplify and accelerate passenger movement and baggage handling. Montréal-Trudeau is a world leader in the field of winter operations, aircraft de-icing and sustainable development. Finally, customer satisfaction is currently at its highest.

Furthermore, divestiture has proved a very efficient form of decentralization. The airport improvement programs are determined based on local needs and priorities, and not on the basis of any political agenda or pressures. Similarly, the administrative autonomy of the local authorities allows rapid decision-making suited to their particular situation, for example in relation to operational needs or commercial development priorities.

Finally, the Canadian model is distinguished by a system of governance that combines professionalism and sensitivity toward the local community. The board of directors, which does not include elected officials or active staff members, is composed of experienced administrators mostly put forward by local authorities; they have a fiduciary role toward the airport authority and collectively possess a set of key skills. In addition, governance of the airports is based on transparency and consultation of stakeholders. Over the years, as a general rule, the authorities have been able to efficiently and harmoniously reconcile the various interests at stake. In its Report of the future growth and global competitiveness of Canada’s airports in June 2012, the Standing Senate Committee on Transport and Communications also rightly concluded that the governance of the airports was adequate.

One more voice that should be heard on this issue is Daniel-Robert Gooch, the former president of the Canadian Airports Council. In a March 2014 article printed in the Globe and Mail, Mr. Gooch wrote:

*Twenty years after the operation of airports was transferred from the federal government to independent local airport authorities, many Canadians still do not realize that the federal government no longer runs our airports. In fact, most are not operated by any level of government. While the federal government retains legal title to the land, most major airports in Canada are operated by non-share capital corporations that are fully responsible for self-funding all operating and infrastructure costs and must invest any profits back into the airport.*

It wasn’t always this way. Until the early 1990s airports were managed by the federal government with civil servants running the business and taxpayers bearing the burden for all capital investments and operational costs not covered by airport charges. With taxpayers directly subsidizing the Canadian transportation system in these times, by the early 1990s the annual cost to taxpayers for operations alone was $135-million a year (with minimal investment in facilities).

To get government out of the business of running airports, operating and funding responsibilities were transferred to local airport authorities under detailed long-term leases that set out the governance and consultation mechanisms under which the airports are run. This model was intended to make airports more like private enterprise, while ensuring they became more responsive and accountable to a broader range of stakeholders through local management.

Under this system, airports have invested more than $19-billion in airport improvements since 1992 with virtually no funding from taxpayers. This is not generally understood. With few exceptions, Canada’s major airports are not subsidized by government. Rather, they pay $280-million a year in rent to the federal government – more than $4.8-billion since 1992 – and hundreds of millions in “payments in lieu of tax” to municipal governments across Canada.

Canada essentially has a “user pay PLUS” system for aviation in which users pay for airport infrastructure, security screening and air traffic control, plus a little extra to the federal government.

In addition to making Canadian airports more pleasant for travellers, with facilities ranked first in the world by the World Economic Forum and regularly winning international awards, these investments mean that our airports are able to handle the doubling of traffic we have seen since 1993.

These investments also have allowed airports to diversify and expand profitable revenue streams through food/beverage, retail, hotels and commercial real estate that have kept in check charges that airports would otherwise pass on to airlines and their passengers. While government-related costs contribute significantly to the relatively high cost of air travel in Canada, the revenue generated from these non-aviation airport ventures ensures Canada’s cost competitive disadvantage is not worse.

With continued concerns about the impact that Canada’s user pay plus approach to aviation has on cost competitiveness, there could certainly be improvements in the system and airports actively contribute to these discussions. However, among those who know and understand the airport model in Canada, the broad consensus is that the model works.

In Canada, we have airports that have invested billions of dollars to ensure they are able to exceed safety and security requirements and meet the demands of ever growing traffic. According to the Conference Board of Canada statistics, we have an air transportation sector with a $35-billion economic footprint and 140,000 directly employed Canadians. Our system works because it balances the needs of all stakeholders. This is good for Canada, air travellers and the communities our airports serve**.**

# Comparison to the rest of the world

So how does our system stack up against the rest of the world? It is a very mixed bag, but here are two quick examples to use as comparators:

1. **United States**

Almost all commercial service airports in the United States are owned by local and state government, or by public entities such as airport authorities or multi-purpose port authorities. In 1996, the American Congress established the Airport Privatization Pilot Program (APPP) to explore the prospect of privatizing publicly owned airports and using private capital to improve and develop them. Participation in the APPP has been very limited. Only two airports have completed the privatization process and one of them later reverted back to public ownership. Owners of other airports considered privatization but eventually chose not to proceed. The lack of interest in privatization in US airports could be the result of readily available financing sources for publicly owned airports, barriers or lack of incentives to privatize or the potential implications for major stakeholder.

The Federal Aviation Administration (US), the body that administers the APPP, is likely to carefully examine privatization proposals that might risk closures of runways or airports, that might reduce aviation system capacity or that might appear to favour certain airport users over others. The APPP has had a very limited success in increasing the number of privately run airports. Since inception 10 airports have applied to enter the APPP and as noted above, only two have completed the entire privatization process.

Of interest is the participation of Chicago Midway Airport, an airport that is comparable to Tier 1 airports in Canada, used the only position reserved for a large hub commercial airport under APPP. On October 8, 2008, Chicago City Council agreed to a 2.5 billion 99-year lease with Midway Investment and Development Corporation, a consortium that was composed of Citigroup Inc. (which owned 50% of Vantage Group in 2008) and the Vancouver Airport Authority (owned the other 50% of Vantage Group in 2008) as well as John Hancock Life Insurance Co. The lease agreement was terminated when the group missed the April 6, 2009 payment deadline. A renewed effort to lease Midway was abandoned in 2013 after one of the two bidding groups dropped out. The City withdrew its preliminary privatization application.

The APPP, over its 20-year history, has not been successful in stimulating wide interest in airport privatization. It is ironic to note that in the United States, a bastion of free enterprise, the big airports are still largely publicly owned.

1. **Europe**

According to a 2010 study by Airports Council International, approximately 13% of European airports are owned by mixed public-private shareholders and 9% are fully privatized. Airport privatization started to build momentum when British Prime Minister Margaret Thatcher’s administration privatized the former British Airport Authority (BAA). The privatization of BAA has not been without its critics. Some economists argued that by selling BAA’s 7 airports all together the UK government had in effect converted public assets into a regulated private monopoly. In 2009 the UK Competition Commission required BAA to divest itself of 3 of the airports in order to maintain a competitive market.

Not all airport privatization has been successful. For example, Cardiff Airport in Wales was bought by a private Spanish consortium but had to be purchased by the Welsh government after passenger traffic fell to less than half of annual passenger traffic and, as a result, the airport became unprofitable. Likewise, Prestwick Airport in Scotland was sold to a private New Zealand operator in 1992. In 2013, it was purchased by the Scottish government in 2013 for £1 after passenger numbers had fallen sharply.

# Options for Privatization

The Emerson Report did not specifically mandate one particular model for further privatization of Canada’s airports. Instead it noted that “a number of options are available for the privatization of the large airports depending on whether the government chooses to maintain full or partial ownership of the land, or fully privatises both the operations and the assets of the airport together.”

The report continues by suggesting the following options:

## Retaining ownership of the airport lands and assets:

“Monetizing” the rent revenue stream under the ground lease by selling it to a private investor who would name directors to the Board instead of the federal government.”

This is not a new idea and even the Emerson report noted problems with this stealth form of privatization. They said that “option would not resolve the identified cost competitiveness or end of lease issues.” Even more than this, this option would literally sell the ground beneath the airport’s feet, and cede control to a private shareholder board of directors.

## Selling the airport lands and operations:

“Converting the existing airport authorities into a share capital, for-profit business corporation under the Canada Business Corporations Act and selling the airport lands to the authorities.”

This would be the full divesture of all airport assets to the private sector. Later, we will speak about the rationale against such a move. For now, we simply note that this is being put forward as an option, primarily at the request of private interests, but with the support of several major Canadian airport authorities.

## Partial sale of the airport lands and assets:

“Forming an equity partnership with a private sector manager who would own at least 49% of the airport and be responsible for its operation under a contract.”

This is a modification of the initial full-sale recommendation. It is what some have called the slippery slope option. Once you sell off half of the airport assets, it is hard to imagine that pressure would not increase to divest of the rest over time.

# Concerns raised by the Emerson report

* Even as they put these additional options for airport privatization forward, the report offers a number of concerns that need to be addressed before they could happen. They include a regulatory regime would be needed to balance the interests of shareholders and users (including passengers and carriers).
* Regulations would be required to ensure that fully privatized airport authorities are restrained from excessive profit taking.
* Regulations to ensure the lowest administrative and cost burden on government, that does not incent ongoing annual increases in fees and profits. (that they note have been observed at the large airports in the United Kingdom.)
* An economic mechanism for regulating prices and tariffs based on the Australian model of self-regulation and a system of arbitration of complaints is also recommended.

# Downside of Change/Privatization

UCTE is of the opinion that privatizing airports involves surrendering control of economically important facilities for Canadians. There are many lessons to be learnt from other jurisdictions who have already gone down that path – and success was limited at best.

Research demonstrates that proponents of privatization are short-sighted in their want to generate revenue from these vital Canadian economic drivers. It is well known that Canadian airports rank amongst the best in the world; they are efficient and infrastructures are well-maintained and regularly upgraded. UCTE strongly believes that not-for-profit status needs to remain in place to solidify the leadership role that Canada places in all realms of aviation.

The current Canadian model for airport management has proven effective with major Canadian airports ranking amongst the best, efficient and whose infrastructures are well maintained and regularly upgraded. Most airports are 100% common-use for improved utilization. Furthermore, financing is simple and expansion projects are tied to community needs and not government agenda. Privatizing airports should not simply be viewed as a short-term revenue raising option for governments. In fact, recent case studies from around the world demonstrate that there is no reason to risk privatizing these critical economic and transportation infrastructure assets.

Further airport privatization is not in the interests of our communities, the travelling public and the people who work at Canada’s airports because:

1. **Increased Costs**

There is a very real danger that despite the promises of would-be investors, that the costs to operate and maintain airports could increase. This has been the experience of other jurisdictions, notably Britain and Australia. In Australia when they sold their airports in the 1990s to private consortiums revenues to government went down and passenger fees increased. In some cases, they were double from before.

In addition, what we have seen in other countries is that the related costs of flying like parking, and airport improvement fees also increased. This has led to a decrease in passenger traffic in airports like Cardiff and Prestwick as we have previously noted. This is a particular concern in Canada since passengers can easily drive to American border towns like Ogdensburg from Ottawa. It could mean both reduced air passenger travel and higher operating costs for airlines.

There is also a potential increased cost to government, even as they hope to gain from a short- term asset sell-off. As Marc Laroche and Craig Richmond have noted, Canadian airports carry a debt of $13.3-billion. Before the airports can be sold to private interests, that debt will have to be factored into the sale price of the assets. In Australia, the government absorbed the airports’ debt in an effort to make the investments more attractive to potential bidders, but at a cost to passengers and taxpayers.

1. **Loss of Revenue**

Since the new airport authority model was introduced, investments in Canada’s airports have been over $19 billion up to 2014. Over that time, the airport authorities have paid several hundred million dollars in rent to Transport Canada. That is far more than the value of the assets transferred at the time of divestiture, and in fact has been a major source of general revenues for the federal government in that period.

The new system has also meant that our airports are run, and maintained without government funding and without the need for additional and often very expensive investments. The reality is that today Canada’s airports contribute more than $1-billion a year in rent and other fees to the government. That revenue would dry up and disappear under airport privatization and would have to be replaced by taxation or cutbacks in government operations.

1. **Passenger Treatment/ Safety**

In a privatized model, the main objective is not passenger safety or convenience. It is profit. This has been one of the major failings of other privatizations in Canada and in other countries. The need to squeeze maximum profit for shareholders becomes paramount. In some other jurisdictions, this has led to a reduced passenger experience as the new for-profit owners seek new ways of reducing their costs. This could mean reducing things such as cleaning and service staff resources and eliminating services such as complimentary Wi-Fi.

We do not know if passenger safety could be compromised under a privatized model, but what are the guarantees? Right now, we have government control and local, community oversight. What would we have if an international corporation, not even headquartered in Canada takes over the operation and maintenance of our airports?

1. **Community/Local Control**

Canada’s airports are self-sustaining businesses that directly benefit their local communities through economic development, tourism and investment. Since the new model was created in the 1990’s airport authorities have invested almost $20-billion in our national airports. Our airports are run by non-political representatives from our local communities who sit on the airport authority boards. Moving to a private shareholder model will eliminate local representatives who ensure that local interests are served. This includes ensuring economic benefits from tourism and investment are retained and returned to the communities and not just to some corporation.

1. **Labour rights**

One of the reasons why the initial transition to the local airport authority model was successful was because all the rights, benefits, terms and conditions of all workers, both union and non-union, were guaranteed under the transfer agreement. Under privatization, all of those rights and benefits would be threatened. In the move to maximize profits under other privatization schemes, one of the first things to be threatened were the salaries and benefits of the existing workforce. Those would certainly be in peril under any airport privatization plan. So too, would be the very right to unionization.

Despite legislative protection other privatization initiatives have led to a de-unionization drive and the ultimate withdrawal of union rights for employees in the new private corporation. This would be a loss to not just the workers who would see their wages decline, but also to the local community that relies on that income to support their local economy. There is also the very real possibility that there would be fewer workers in a privatized airport that would greatly impact the spin-off and supporting jobs in the affected communities.

# Moving Forward

UCTE is open to listening to all possible improvements to the Canadian airport model, however in our view, there are simply too many risks and not enough rewards to justify further privatization of Canada’s airports. The long-term disadvantages outweigh any possible benefits that may be achieved by the privatization of public assets. UCTE strongly believes that not-for-profit status needs to remain in place for all airports. Let’s keep the hen that lays the golden eggs.

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