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About the National Roundtable on Travel and Tourism (NRTT)

The National Roundtable on Travel and Tourism is made up of the Tourism Industry Association of Canada, the National Airlines Council of Canada, the Canadian Airports Council, the Hotel Association of Canada and the International Air Transport Association. Together these sectors are responsible for employing 1.6 million Canadians or 1 in 10 Canadian workers.

As one of Canada's most important and strategic economic sectors, the NRTT's mission is to promote innovative public policy that enhances the global competitiveness of Canada's Travel and Tourism Industry and ensures its future positioning as one of the leading players in the worldwide travel and tourism market.

Big Picture: Aviation's Impact on the Economy

Breadth and Depth of Travel Industry in Canada

In Canada, travel and tourism is worth $84 billion dollars a year and creates economic activity and jobs in every region of the country. There are over 618 000 Canadians employed directly by tourism spending (about 200 000 are under 25 years old) and over 157 000 businesses. The sector is Canada's number one service export with over $18 billion in foreign receipts in 2013 and contributes an estimated $9.6 billion a year to federal coffers.[1]

Aviation is a key part of Canada's travel and tourism sector. Overall, aviation directly employs 141 000 people and has an economic footprint of $35 billion in GDP. Air Canada, Air Jazz, Transat and WestJet, (some of the largest carriers of international visitors and leisure travellers) alone employ 46 000 people and carry over 50 million passengers every year.[2] Canada's airports directly support over 63 000 jobs and generate almost $12 billion in GDP every year.[3]

Mobility Economy as a Path to Export for Canada

Canada is a trading nation. Our abundance of natural resources, large land mass and relatively small population dictates that economic prosperity is contingent upon enhancing trade with other nations. Canada's trade policies seek to enhance the movement of goods, capital, and people across our borders. While much has been accomplished to augment this movement, many obstacles remain that limit the movement of people. Although air travel is a key impediment, Canada also needs to enable the seamless movement of travellers across transportation modes (air, trains, ferries, etc.) to enhance the efficiency of economic mobility.

Facilitating connectivity feeds what the Tourism Industry Association of Canada (TIAC) has called the "mobility economy." By simplest definition the mobility economy is the movement of people for the

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[1] Tourism Industry Association of Canada, Annual Report 2014
http://tiac.travel/_Library/TIAC_Publications/TIAC_Annual_Report_EN_FINAL.pdf

[2] National Airline Council of Canada, http://airlinecouncil.ca/en/who-we-are.html

[3] Conference Board of Canada, The Economic Impact of the Air Transportation Industry in Canada, http://www.cacairports.ca/sites/default/files/Docs_2013/CAC_Economic-Impact-Study_FINAL_April-2013.pdf

purpose of business or leisure travel and the expanded economic opportunities that come with these new connections. Capital is not patriotic and seeks the highest return through the path of least resistance: those countries that gain efficiencies in facilitating trade achieve a competitive advantage.

Intuitively, people do business with people they know and interact with. This is shown in a recent econometric study by Deloitte, which found that countries that experience higher levels of reciprocal travel create increased trade and investment. Deloitte quantifies that every 1% increase in international arrivals to Canada stimulates over $800 million in broader exports with our trading partners.[4]

Global Tourism Competition: Canada's rankings and opportunities

Canada's competitive edge on the world tourism stage has suffered in recent years. Canada has fallen from the 7th most visited country in the world in 2002 to the 17th, lost 4 million international travellers per year and is growing at a mere third the rate of the rest of the world. Canada's loss of international visitors is concerning. In 2013 international visitors accounted for only 21% of travellers in Canada– this is down from about 33% in 2000. International travellers are not only good for tourism businesses' bottom line (international visitors stay longer and spend more) but a good visitor mix diversifies the market and lowers risk for investors.[5]

INTERNATIONAL TOURIST ARRIVALS Top 20 Countries – in Millions				
Rank	**2002**		**2013**	
1	France	77.0	France	NA
2	Spain	52.3	U.S.	69.8
3	U.S.	43.6	Spain	60.7
4	Italy	39.8	China	55.7
5	China	36.8	Italy	47.7
6	U.K.	24.2	Turkey	37.8
7	**Canada**	**20.1**	Germany	31.5
8	Mexico	19.7	U.K.	31.2
9	Austria	18.6	Russian Fed.	28.4
10	Germany	18.0	Thailand	26.5
11	Hong Kong	16.6	Malaysia	25.7
12	Hungary	15.9	Hong Kong	25.7
13	Greece	14.2	Austria	24.8
14	Poland	14.0	Ukraine	24.7
15	Malaysia	13.3	Mexico	23.7
16	Turkey	12.8	Greece	17.9
17	Portugal	11.6	**Canada**	**16.6**
18	Thailand	10.9	Poland	15.8
19	Ukraine	10.5	Macao (China)	14.3
20	Netherlands	9.6	Saudi Arabia	13.2

[4] http://tiac.travel/_Library/TIAC_Publications/Deloitte_Passport_to_Growth_-_Nov_2013.pdf
[5] Tourism Industry Association of Canada, Annual Report 2014, http://tiac.travel/_Library/TIAC_Publications/TIAC_Annual_Report_EN_FINAL.pdf

Impact of Aviation Challenges on Competitiveness

In almost all aviation markets, cost is king and the high cost of flying to and within Canada is a barrier to travel. In fact, the World Economic Forum rates Canada's price competitiveness at 124th out of 140 countries mostly due to our high input costs in the form of ticket taxes and charges (136/140).[6] A 2011 Canadian Tourism Commission study looking at international travellers' perception of Canada as "a destination that is affordable to get to by air" shows that high airfares act as barriers for travellers from some of our most important long haul markets: only 39% of travellers from the UK think that the cost of air travel to Canada is reasonable. The same is true for 27% of Germans, 19% of Japanese, 26% of South Koreans and 32% of Australians.[7]

From an economic standpoint, the price sensitivity (demand elasticity) of travellers has been well studied. While it is generally accepted that business travellers have lower sensitivity than leisure travellers, IATA has released a report that details other insights on travel elasticity:

- Since the global advance of Low Cost Carriers (LCCs), passengers are more price sensitive than they were previously.
- In many cases, air transport is more elastic than other aspects of travel (attractions, restaurants and lodging)
- Residents of developing countries are typically more sensitive to price[8]

The repeal of the BC fuel tax on international flights is another case study that quantifies the impact of what may seem, at first glance, a "small" fee. In BC the jet fuel tax was comprised of the fuel tax rate (2¢) and GST (5%) but was repealed in April 2012. Since then it is reported that 22 airlines have added flights to Vancouver. The government estimates that the $12 million in initial lost revenue has been replaced by new payroll and consumption taxes to the tune of about $20 million.[9]

High fees and taxes are causing Canadians to look for alternatives. The Canadian Airports Council released a report that estimated more than five million Canadians cross over to U.S. border in search of cheaper flights. U.S. border airports are certainly capitalizing on their competitive advantage: Canadians make up almost half (46%) of passengers at Buffalo Niagara International Airport and up to 70% of passengers at the Niagara Falls International Airport.[10]

[6] WEF, Travel and Tourism Competitiveness Index, 2013
[7] CTC, Global Tourism Watch 2011- Global Summary Report http://en-corporate.canada.travel/sites/default/files/pdf/Research/Market-knowledge/Global-tourism-watch/global_summary_gtw_yr5_2011_en.pdf
[8] IATA, Air Travel Demand: Measuring the responsiveness of air travel demand to changes in prices and incomes. IATA Economics briefings No. 9
[9] http://www.cbc.ca/news/canada/toronto/fuel-tax-hike-will-likely-push-airfares-higher-officials-say-1.2712843
[10] http://www.theglobeandmail.com/report-on-business/international-business/buffalo-airport-trumpets-tax-savings-to-win-more-canadian-fliers/article21205763/ For Niagara Falls: http://www.gillibrand.senate.gov/newsroom/press/release/with-increased-international-passengers-flying-through-wny-airports-gillibrand-urges-tsa-to-bring-pre-check-program-to-niagara-falls-and-buffalo-niagara-

Current Market in Canada

What is Working

Overall, Canada has a great reputation as a place to visit and do business. The Government of Canada has made important steps in easing visitor documentation requirements and supporting nature attractions and cultural events. Canada is also getting some things right in terms of its aviation system. For example, the World Economic Forum ranked Canada the best in the world in terms of air transportation infrastructure.[11]

The government has also shown a willingness to work with the industry to ensure competitiveness. Two recent examples include the ratification of the Cape Town Convention to reduce air carrier financing costs as well as changing requirements for flight attendants to put Canadian carriers on equal footing with their competitors.[12] There has also been encouraging progress on easing visitor documentation requirements such as the facilitation of online applications, investment in new Visa Application Centres (VACs), the CAN+ and other fast-track programs, lifting visas for Chilean visitors and, in some respects, the Electronic Travel Authorization (eTA).

Canada's Unique Challenges

Unique User Pay System

Since the early 1990s, Canada's aviation system has been improved by the privatization of the country's primary airlines, air navigation system (NAV Canada) and the corporatization of airports. This move away from government control was furthered by the 2001 review of the *Canada Transportation Act* which emphasized a "user-pay" model that would send "the right pricing signals to transport users [and] will lead to the right amount of use and the right distribution among modes." The shared public infrastructure facilities would also "include direct user input in decisions on funding and spending."

While the privatization and corporatization models have helped to put industry experts in decision making positions, it is the NRTT's opinion that the system has moved from "user pay" to "user pay plus," with excise-level taxes collected on input costs throughout the value chain. This added pressure on input costs is hurting Canada's competitiveness as a place to visit and do business and lowers the value proposition for users.

While the user pay system has many advantages in theory, a re-visitation of the system is long overdue to improve industry competitiveness relative to other countries and ensure users are receiving value for the money they are spending on the system in user fees and taxes. Indeed the system should be re-considered through the principles set out in the *User Fees Act* (Bill 212), specifically Section 7: "a

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international-airports- ***or*** http://www.tampabay.com/news/business/allegiant-air-to-start-flying-from-st-petersburg-clearwater-to-niagara/1192590

[11] WEF, Travel and Tourism Competitiveness Index, 2013

[12] CBOC, A New National Air Transportation Policy, p.3-4.

regulator authority may not fix, increase, expand the application of or increase the duration of a user fee unless the result gives an additional benefit to clients."[13]

Competition with the U.S.

In the travel and tourism industry, the U.S. plays dual roles of being a competitor as well as a customer and a key challenge on both these fronts is that it can be much cheaper to fly in the U.S. than Canada.

Not only is Canada losing U.S. visitors –Canada has lost over 3.5 million U.S. visitors a year since 2002—we are losing visitors *to* the U.S. While Canada experienced a "lost decade" from 2002-2013, the U.S. experienced a 36% increase in visitation in the same period. With a $200 million investment in their marketing agency Brand USA, visa reforms and cheaper airfares, it is easy to see why visitation to the U.S. has stayed robust with an increased by 4.6% while Canada only saw a 1.5% increase in visitors in 2013.[14] Furthermore, Canada must also compete with the U.S. for Canadian outbound travel. Every year approximately 5 million Canadians drive to border airports in the U.S. to fly outbound—an opportunity that the U.S. is aggressively pursuing with marketing campaigns and subsidizing airport expansions.

Case Study: Canada vs U.S.

While there are instances and anecdotal evidence that flights to and within the U.S. are more expensive than Canada, a number of studies show that the overall average shows a definite price differential in the U.S.'s favour:

- *Driven Away: Why More Canadians are Choosing Border Airports* by the Conference Board of Canada does an in depth study of price differentials between U.S. and Canadian flights by examining differences in both base fares and taxes and fees.
    - Case studies from Canadian versus U.S. border airports to Los Angeles, San Francisco, Las Vegas, New York and Orlando show that differentials in base fares where anywhere from 20% to 96%. The higher base fares are attributable to factors such as air carrier cost structure (compensation, fuel and aircraft ownership costs, navigational charges etc.) as well as taxes and fees such as airport rents that make their way into landing fees charged to airlines.
    - When comparing fees and taxes that apply to the base fare the study found that Canadian fees and taxes contribute to roughly 40% of air fare difference.[15]
- The Senate Standing Committee on Transport found that on a national scale the difference between Canadian and American roundtrip flights averaged $428 per passenger with taxes, fees and charges accounting for 15-33% of the difference.[16]
- The same committee report found that 43% of the price of the flight from a typical Canadian airport consisted of taxes and fees (including airport rent) while a similar flight from a U.S. border airport consisted of only 14% in taxes and fees

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[13] http://www.parl.gc.ca/HousePublications/Publication.aspx?DocId=2331625&Language=E&Mode=1&File=39
[14] TIAC, Annual Report 2014
[15] Conference Board of Canada, "Driven Away – Why more Canadians are Choosing Border Airports"
[16] Standing Senate Committee on Transportation and Communications, The Future of Canadian Air Travel: Toll Booth or Spark Plug? June 2012.

- In its case studies, the Montreal Economic Institute found:
    - Montreal to Fort Lauderdale compared with Plattsburg to Fort Lauderdale found a 36% difference ($247 more from Canada),
    - Similarly flight to New York from Montreal was 10% more expensive than from Burlington.[17]

Roles and Responsibilities in a User Pay Model

While the privatization and corporatization of the aviation industry have created great efficiencies, the system has become "user pay plus" since 1994 when the user fee model was introduced. The creep to "user pay plus" is driving up the cost of air transportation in Canada which is hurting our competitiveness in travel and tourism as well as export industries in other sectors that have to compete in a hyper-connected marketplace.

What are the appropriate roles of industry, direct users and government? When considered closely the aviation industry has an impact far beyond those who just fly from destination to destination. As 9/11 demonstrated, the security of the aviation system is in the best interest of all Canadians. So too, is an accessible transportation network for international businesses and investors. Unfortunately, the Canadian Government's devotion to the user fee concept has become fanatical since the privatization of the aviation industry over 20 years ago creating an imbalance in input costs that are hurting Canada's competitiveness.

Aviation Cost Structure:

Fee[18]	Gov't Revenues	User Pay	GST
Airport Ground Rent	$282.4M		$14.1M
Air Transport Security Charge (ATSC)	$635.6M		$8.0M*
Fed. Excise Tax on Jet Fuel	$97.2M		$3.5M*
NAV Can Fees		$1.18B	$35.1M*
Airport Improvement Fees		$921 M	$46.0M
User Fees	$2.1 billion		
GST on User Fees	$81.2 million		
Government Fees + GST	$1.04 billion		

The government collects over $1 billion in fees plus $106.8 million in GST on government and user fees. For a further break-down, Dr. Fred Lazar does an in-depth and cumulative study of the cost of government policies in *The Economic Impacts of the Member Carriers of the National Airlines Council of Canada*.

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[17] Montreal Economic Institute, Canada's High Airfares and Passenger Leakage, March 2014.
[18] Airport Ground Rent: Public Accounts of Canada 2013
NAV Can: Transportation in Canada Addendum 2013 (Domestic 35770000 transborder 23815000 from domestic $14.67 average charge, U.S. $7.50 average charge (CTC estimate))
ATSC: Public Accounts of Canada 2013. **GST is only collected on transborder and domestic ATSC charges, $8 million is CTC's estimate from 2010 numbers, when total collected was $35million less.
Excise on Jet fuel: ** GST Estimate based on Domestic/Transborder = 72% of all passengers
Airport Improvement Fees: Transportation in Canada Addendum 2013 (2012)

A detailed look at how high input costs work will help to further clarify roles and responsibilities of the stakeholders in this sector.

Ground Rents & Airport Improvement Fees (AIFs)

User Fees…Plus: While the pure concept of user fees would mean service levels would increase with fees, there has been a creep of government fees and taxes that are not making their way back into the system. The end result is that taxpayers are paying more for less value. For example, grounds rents (plus GST) were instated to recoup the government's initial investment and "improve the federal government's financial position."[19] At the time of transfer the assets were valued at $2.9 billion (2012 $), but to date the airports have paid $5 billion in rent to the government[20] – that is a $2.1 billion overpayment that has not been reinvested back into aviation.

Disincenting Independent Revenue Generation: Generating revenue from supplemental means (retail tenants, parking garages etc.) is, in some cases, not as competitive a strategy for airports as it would be for traditional businesses because the airport's gross revenue is factored into the airport's rent (plus GST). Even a 10% airport rent formula is much less profitable than a 26% statutory tax rate (see box).

Example of how rent formula hurts the consumer, by disincenting the airport from collecting ancillary revenue [21]	
Parking garage costs $250/day to operate; how much would $50 profit cost the airport?	
Rent Formula: 10% on Gross Revenue	**Corporate Tax**
• Gross revenue is taxed	• Only profit is taxed
• If garage makes profit i.e. has revenues of $300, all $300 is taxable	• If garage makes profit i.e. has revenues of $300, only $50 is taxable
• 10% rent charged on gross revenue	• Statutory Corporate Tax Rate 26%
• **$30 in taxes, $20 in "take home"**	• **$13 in taxes, $37 in "take home"**

Rent and AIFs are Countervailing Forces that Cost the Consumer: Further complicating the loss of revenue due to ground rents, is the nature of the lease agreement between airports and the government which gives the airport authorities a not-for-profit, non-share capital status. Revenue from aeronautical charges and ancillary revenue from food, retail and other services is insufficient on its own to cover capital infrastructure costs, which is why Canadian airports have Airport Improvement Fees, which are similar to passenger facility charges in other countries. As the rent formula is based on gross revenue, the government collects rent (plus GST) on any AIFs raised. In 2012, around $100 million in rent attributable to AIFs and $45 million in GST was collected by government. The AIF/rent cycle is a quagmire that perpetuates itself – but still costs the consumer.

[19] National Airports Policy, https://www.tc.gc.ca/eng/programs/airports-policy-nas-1129.htm
[20] Conference Board of Canada, A New National Air Transportation Policy
[21] Example from C.D Howe Institute: Full Throttle: Reforming Canada's Aviation Policy, P. 10

Air Traveller Security Charge: User Fee or Profit Centre?

For a user pay model to work and be competitive, the user fees must reflect the services provided and cash flow needed. In 2014, 53.9 million passengers were screened by CATSA, up 5.7% from 2010. This increase in demand (passengers needing screening) has been met with 9.6% decrease in CATSA funding over the same time period.[22] This discrepancy in revenue collected (more) and service provided (less) moves the model from an efficient and cost saving “user fee” to a “user fee plus” revenue stream.

A safe and efficient aviation system benefits all Canadians as well as our domestic and international economic links. Users must receive value both in terms of security precautions and efficient passenger experience for the fees they pay.

Economies of Scale

Transportation by air in a country as big and sparsely populated as Canada is not a luxury but is essential to supporting Canada’s economy, as well as maintaining economic and social cohesion. However, flying is expensive and economies of scale in our market mean there isn’t always enough demand to support the high competition/lower price environments we find in the U.S., Europe and other regions with high Low Cost Carrier (LCC) penetration.

Fighting Economies of Scale through Hub Traffic

As a sparsely populated yet geographically vast country, Canada consistently struggles with issues surrounding economies of scale. Canadian traffic alone will never generate enough demand to lower prices to put us on equal footing with the U.S. or with Europe’s LCCs. However, Canada can take advantage of its location between the Americas and Europe/Asia to boost fly-through traffic (and competition) by taking advantage of its natural geographic position as a gateway. Transiting passengers increase traffic enough to support new long haul routes or increased capacity on existing routes, which increases competition and Canada’s connectivity to the world. A U.K. study found that increased direct flights have a direct impact on trade volume with developing countries.[23]

Modernizing our travel documentation system to allow for more Transit Without Visa and Electronic Travel Authorization-free transiting would make Canadian airports more attractive hubs and potentially provide Canada with a competitive advantage over the U.S. for some transit passengers. Currently, U.S. airports handle one and a half times the number of passengers per capita that Canadian airports do.[24] However, in five years, U.S. airports are projecting that twenty of the nation’s top airports will experience “Thanksgiving-type congestion” (i.e. up to 259% higher than current average) two days a week year round.[25] When compared to crowded U.S. airports with lower ranked infrastructure, Canada has room to grow.

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[22] NACC
[23] Frontier Economics. Connecting for Growth: The role of Britain’s hub airport in economic recovery. Sept 2011.
[24] Conference Board of Canada, A New National Air Transportation Policy, i.
[25] USTA. Thanksgiving in the Skies: An annual look at the Future of Air Travel in America, November 2014.

Recommendations

Creating More Customer Value

A common fear from government is that reductions in fees and costs will only serve to boost aviation stakeholders' bottom line. NRTT believes that travellers will be the beneficiaries of any tax or fee relief from the government.

Reducing the input cost burden borne by the air transportation industry would improve its overall competitiveness, entice new entrants to the Canadian market, and allow existing air carriers to re-invest any potential savings into training, fleet renewals, and the development of new routes and markets for travellers.

Indeed, history has shown that the Canadian aviation industry has managed to pass on productivity and cost savings to their customers through lower relative ticket prices. The Canadian Passenger Air Services Price Index (Table 329-0078) shows a downward trend of 3.1% between 2006 and 2012.[26]

Economists at the Conference Board of Canada note that the higher the level of competition the more savings are likely to be passed on to customers[27] – and with the influx of low cost carriers and U.S. border airports, it stands to reason that now, more than ever, the aviation industry will respond to tax and fees cuts in a way that benefits the average traveller.

National Roundtable on Travel and Tourism (NRTT) Recommendations

Aviation is vital to the prosperity –both economic and social – of a country the size of Canada. The current emphasis on input costs in the form of inflated user fees is akin to an excise tax even though air travel is neither a luxury nor a "sin." The NRTT recommends the following measures to create a more competitive aviation cost structure:

General Impact of Aviation

1. That the panel consider the how the aviation industry works in tandem with destination marketing, traveller documentation rules and product investment as an integral part of supporting Canada's wider services and trade-based economy .

Value Standards and User Pay Plus Model

2. That the panel consider the nation-wide role of aviation as an economic enabler and re-evaluate the roles and responsibilities of travellers, the public, government and industry.
    a. Reconsider the structure and, more broadly, the existence of airport rent. NRTT recommends immediate incremental reduction in airport rents through a restructuring of the rent formula including omitting non-aeronautical revenue from formula with the ultimate goal to eliminate rents completely.

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[26] Statistics Canada. The Canadian Passenger Air Services Price Index (Table 329-0078) shows a downward trend of 3.08% between 2006 and 2012.

[27] Conference Board of Canada, A New National Air Transportation Policy, p.9

b. Re-evaluate the value received in exchange for user fees. For example, the increased revenue collected via the ATSC do not align with budget reductions for CATSA that have created lower service standard levels for an increasing number of passengers. Users should receive value for the money they spend that is designed to support services.

3. That the panel explore how Canada can better take advantage of its geographic position between Asia/Europe and the Americas to capture a greater share of growing traffic between these regions.

   a. Simplification of the visa process and expansion of Transit Without Visa are fundamental to being globally more competitive in these areas.