



DOMESTIC AIR CARRIER POLICY



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HOUSE OF COMMONS

**NINTH REPORT
STANDING COMMITTEE
ON TRANSPORT**

Maurice A. Dionne, M.P.
Chairman

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House of Commons.
Standing Committee on
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Tuesday, March 23, 1982
Thursday, March 25, 1982
Tuesday, March 30, 1982

Le mardi 23 mars 1982
Le jeudi 25 mars 1982
Le mardi 30 mars 1982

Chairman: Maurice A. Dionne

Président: Maurice A. Dionne

*Minutes of Proceedings and Evidence
of the Standing Committee on*

*Procès-verbaux et témoignages
du Comité permanent des*

Transport

Transports

RESPECTING:

CONCERNANT:

The document entitled, "Proposed
Domestic Air Carrier Policy (Unit
Toll Services), August 1981"

Le document intitulé «Politique concer-
nant le transport aérien intérieur
(Services à taux unitaires), août 1981»

INCLUDING:

Y COMPRIS:

The Ninth Report to the House

Le neuvième rapport à la Chambre

First Session of the
Thirty-second Parliament, 1980-81-82

Première session de la
trente-deuxième législature, 1980-1981-1982

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(Quorum 11)

Le greffier du Comité

Santosh Sirpaul

Clerk of the Committee

Pursuant to Standing Order 65(4)(b):

On Tuesday, March 23, 1982:

Mr. Flis replaced Mr. Penner;

Mr. McRae replaced Mr. Dionne (*Chicoutimi*).

On Tuesday, March 30, 1982:

Mr. Forrestall replaced Mr. MacKay;

Mr. Reid (*St. Catharines*) replaced Mr. Siddon;

Mr. Gourd replaced Mr. Campbell (*LaSalle*).

Conformément à l'article 65 (4)b) du Règlement:

Le mardi 23 mars 1982:

M. Flis remplace M. Penner;

M. McRae remplace M. Dionne (*Chicoutimi*).

Le mardi 30 mars 1982:

M. Forrestall remplace M. MacKay;

M. Reid (*St. Catharines*) remplace M. Siddon;

M. Gourd remplace M. Campbell (*LaSalle*).

CONTENTS

The Standing Committee on Transport has the honour to present its

NINTH REPORT

In accordance with its Order of Reference of Tuesday, December 15, 1981, the Committee has studied and made recommendations relating to the document issued by Transport Canada entitled "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981".

The Committee held public hearings on this matter in Ottawa during 24 sessions between January 28 and March 2, 1982 and heard a total of 48 witnesses. The Honourable Jean-Luc Pepin appeared *in camera* at the Committee's request on February 25. The Committee received 13 written submissions from various parties. The list of witnesses who appeared before the Committee is contained in Appendix A and the list of submissions is in Appendix B. The contributions of those who participated in the hearings were invaluable to the study.

The Committee wishes to express its appreciation to Santosh Sirpaul, Clerk of the Committee, who arranged its hearings and co-ordinated the work, as well as providing procedural advice, and to Marie-Josée Brière of the Translation Bureau, who translated the report. The Committee is also indebted to its advisory staff, which was brought together for the task by the Parliamentary Centre and which comprised Peter Dobell, Timothy Denton, Gregory Kane, Robert Obadia and Cary Swoveland.

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This chapter has been achieved within a regulatory framework established by legislation through a combination of governmental policy statements, decisions of the Canadian Transport Commission (CTC) and decisions on appeal to the Minister of Transport and the Governor in Council. The Commission is convinced that this evolutionary process should not be confined. Rather, it should remain flexible to permit continuing innovation and adjustment to changing market demand and technical developments.

The policy paper presented by Transport Canada was characterized by a departmental representative as "an attempt to live with the status quo" (110). While several witnesses, notably the carriers, limited their remarks to commenting on the specific recommendations contained in the policy paper, a number of others expressed concern that Transport Canada's approach would achieve minimal improvements. Some witnesses went further and suggested the abandonment of all economic regulation, in favour of exclusive reliance on market forces.

* This refers to page 1 of Part No. 11 of the Minutes of Proceedings and Evidence of the Standing Committee on Transport. Subsequent references follow a similar format.

Chapter 1

INTRODUCTION

As background to the examination of the Transport Canada policy paper, the Committee undertook a review of the development of domestic air policy in Canada, with particular emphasis on changes during the last fifteen years. The Committee was favourably impressed by the changes that have occurred during these years, which have led to the establishment of a strong and adaptive air industry that serves the country well.

This adaptation has been achieved within a regulatory framework established by legislation through a combination of governmental policy statements, decisions of the Canadian Transport Commission (CTC) and decisions on appeal to the Minister of Transport and the Governor in Council. The Committee is convinced that this evolutionary process should not be confined. Rather, it should remain flexible to permit continuing innovation and adjustment to changing market demand and technical developments.

The policy paper presented by Transport Canada was characterized by a departmental representative as “an attempt to fine tune the status quo”. (41:5)* While several witnesses, notably the carriers, limited their remarks to commenting on the specific recommendations contained in the policy paper, a number of others expressed concern that Transport Canada’s approach would inhibit future improvements. Some witnesses went further and suggested the abandonment of all economic regulation, in favour of exclusive reliance on market forces.

* This refers to page 5 of Issue No. 41 of the “Minutes of Proceedings and Evidence of the Standing Committee on Transport”. Subsequent references follow a similar format.

After careful reflection, the Committee decided not to limit its recommendations to detailed comment on the policy paper. Rather, the Committee concluded that it should widen its focus and offer its own recommendations on the framework of domestic air policy in Canada.

Main Issues

The Committee believes that there are three major issues that must be resolved in formulating a new domestic air carrier policy.

- 1) **Regulation vs. deregulation:** Will the public interest be better served by a policy that maintains an environment of controlled competition or by one that moves toward the total elimination of economic regulation, along lines similar to those being followed in the United States?
- 2) **Structure of the industry:** Should the future policy encourage a more competitive industry? If so, how rigid should the definition of the role of each group of carriers be?
- 3) **Guidance to the CTC:** If the industry is to continue to be regulated, what guidance should be provided to the CTC to assist it in discharging its responsibilities?

Several witnesses expressed the view that other issues could also affect domestic unit toll air policy: domestic charter services, international services, the role of Air Canada, operating subsidiaries and the role of provincial governments in air transportation. The Committee has taken account of these views in analyzing the issues and formulating its recommendations.

The Committee welcomes this opportunity to review and comment on the proposed domestic air policy prior to its consideration by the government and has responded constructively to the opportunity and the challenge. The hearing process, with open meetings and wide-ranging discussion, provides an excellent means of examining policy proposals. The Committee offers this report as its contribution to the development of policy and considers that the exercise represents an example of productive and co-operative committee work.

Chapter 2

THE DOMESTIC AIR CARRIER INDUSTRY

This section provides a brief description of the Canadian air carrier industry, with particular attention to recent changes that have an important bearing on the major policy issues.

Air carriers in Canada have traditionally been divided into three groups: national, regional and local carriers.

National Carriers

After a period (1943-1958) when Air Canada operated on transcontinental routes without competition, a first step toward the recognition of two national carriers took place in 1958, when CP Air was allowed to compete with Air Canada on the Vancouver-Winnipeg-Toronto-Montreal route. The amount of competition permitted between CP Air and Air Canada was increased in 1967, 1977 and 1979. The changes in 1979 removed all remaining restrictions on the competitive relationship between Air Canada and CP Air.

Although the role of the national carriers has not been explicitly defined by government policy, it is evident that they perform an omnibus role, serving many different types of routes in southern Canada using a wide variety of jet aircraft.

Regional Carriers

Policy statements in 1966 and 1969 defined and identified the roles of five regional carriers: Eastern Provincial Air (EPA), Nordair, Quebecair, Transair and Pacific Western Air (PWA).

Regional carriers were to operate local and regional routes to supplement the domestic mainline operations of Air Canada and CP Air and to provide regular, scheduled services into the north. Their services were to be on routes that did not fit mainline operations. In some cases, these routes were to be transferred from the nationals.

Regional carrier operations were to be conducted within assigned regions: EPA in the Atlantic provinces with access to Montreal; Quebecair in Quebec from Montreal east; Nordair in eastern Ontario and northwestern Quebec; Transair in the prairie provinces and northwestern Ontario with access to Toronto; and PWA in British Columbia and western Alberta. Under certain circumstances, the operations of a regional carrier could extend into the area of an adjacent regional carrier. Limited competition was to be allowed between regional and national carriers where warranted by market demand and efficient operation of a specific route and by the suitability of the route for the aircraft operated by the regional carrier.

The regionals were permitted to operate domestic and international charters, but such operations were not to overshadow their domestic unit toll operations. They could also provide new types of services in their respective areas or on routes served by the nationals.

Under the Regional Air Carrier Policy, the regional carriers enjoyed rapid growth in the buoyant market conditions that prevailed well into the 1970s. The four regional carriers (reduced from five as a result of the acquisition of Transair by PWA) now operate 46 B-737 jet aircraft and a few twin turbo-prop aircraft. They operate mainly short haul passenger services in southern Canada, although Nordair and PWA also fly passengers and cargo into the north. In addition, all of the regionals are involved to some extent in domestic and international charter operations.

Local Carriers

The role of local carriers has never been explicitly defined by government policy. At present, this group consists of about 75 carriers, varying greatly in size and providing a wide variety of services (passenger and cargo unit toll services, charter and specialty services) in all parts of Canada. The locals operate on short haul, low density routes and a few higher density routes. Local carriers are largest and most numerous in Ontario, western Canada and northern Canada. The equipment operated by the locals ranges from small single engine aircraft to 50-seat turbo-props and a few larger aircraft (Lockheed Electra, Cargo DC-8).

Wardair

Wardair Canada is unique because it does not fit into any of the three groups of carriers described above. Wardair is a charter carrier operating almost exclusively in the international charter market. Its total share of all international charters operating to and from Canada is about 50 per cent.

In 1980, Wardair began operating domestic Advance Booking Charters (ABCs), concentrating mainly on transcontinental operations between Toronto and western Canada. These operations are quite limited, having accounted for only five per cent of Wardair's total activity in 1980.

Recent Changes

In the last five years there have been significant changes in the structure of the domestic airline industry. These changes have resulted from decisions of the Air Transport Committee, decisions on appeal and government policy statements. As a result, the degree of competition among carriers in the domestic market has increased substantially during this period. CP Air has gained improved access to transcontinental and mainline routes; domestic ABCs were introduced; increased competition has been permitted between nationals and regionals; and several local carriers have experienced rapid growth. In the three-year period 1977-1980, the proportion of high density markets (over 70,000 trips annually) served by more than one carrier increased from 70 per cent to 83 per cent; for medium density markets (10,000 to 70,000 trips), the proportion increased from 35 to 46 per cent.

The regional air carriers' current situation is substantially different from what it was when the Regional Air Carrier Policy was promulgated in the late 1960s. There have been two major developments:

- 1) **Involvement of governments:** PWA was purchased by the government of Alberta in 1976, Nordair was acquired by Air Canada in 1978, and in 1981 the government of Quebec became financially involved in Quebecair.
- 2) **Territorial boundaries:** Recent decisions by the CTC and successful appeals to the Minister of Transport have rendered the Regional Air Carrier Policy obsolete. EPA is now authorized to operate non-stop service from Halifax to Toronto, Quebecair was awarded Montreal-Toronto, and PWA was given access to Toronto via Calgary and Brandon.

Local carriers have expanded the range of services that they provide, and some of them have reached a level of development similar to that of the regional carriers in the late sixties.

Chapter 3

THE REGULATORY PROCESS

The *National Transportation Act* and the *Aeronautics Act* govern the regulation of the airline industry.

The policy set out in the *National Transportation Act* establishes the considerations governing the deliberations of the Canadian Transport Commission. It calls for "... an economic, efficient and adequate transportation system making the best use of all available modes of transportation at the lowest total cost". It requires each mode of transport to compete freely with other modes of transport, to bear a fair proportion of the real costs imposed on taxpayers by that mode, and to be compensated for the services it provides as a public duty.

The detailed provisions describing the control of aeronautics in Canada are set out principally in the *Aeronautics Act* and the regulations made pursuant to that Act. The *Aeronautics Act* sets out, in separate parts, the respective powers, duties and responsibilities of the Minister of Transport and the Canadian Transport Commission.

The Minister of Transport has the responsibility, among other things, to supervise the airline industry and carry out such specific duties as the construction and maintenance of airline terminal facilities and the enforcement of safety standards in air carrier operations.

The Canadian Transport Commission has been given explicit powers to regulate the aeronautics industry on matters such as entry and exit, rates and fares, and the terms and conditions of service. These powers, set out in broad terms in Part II of the *Aeronautics Act*, have been supplemented by detailed provisions in the Air Carrier Regulations enacted

pursuant to it. These regulations contain detailed provisions relating to matters such as the classification and grouping of commercial air services and air carriers, licences, changes of control, mergers, charter rules, tariffs and tolls, and various requirements to record and file information with the Commission.

The most important power possessed by the Commission is to issue a licence to operate a commercial air service. The Commission is not allowed to issue a licence "... unless it is satisfied that the proposed commercial air service is and will be required by the present and future public convenience and necessity."

When the Commission issues a licence, it has the additional power to prescribe the routes that may be followed or the areas to be served and can attach conditions to the licence that it considers necessary or desirable in the public interest. The Commission also has the power to suspend, cancel or amend any licence, where public convenience and necessity so require.

The provisions relating to the rates, as well as the terms and conditions of service (technically, tariffs and tolls), are found in the regulations. The criteria that govern the Commission's consideration of fares and terms and conditions of service include such notions as fares being "just and reasonable".

The *National Transportation Act* provides for appeals from decisions of the CTC to the Minister of Transport in the case of licensing decisions, and to the Governor in Council to vary or rescind any order of the CTC. The Commission is obliged to comply with the decisions of these appeal bodies. Appeals are also possible to the courts on matters of law or jurisdiction.

There are three levels to the legal hierarchy: the governing legislation, the regulations that have been made under powers in the governing legislation, and policy statements which are intended to guide the regulator in the exercise of his discretion. The ultimate responsibility for policy guidance rests with the Canadian government. This is normally offered through periodic statements issued by the Minister of Transport. Although neither the *National Transportation Act* nor the *Aeronautics Act* provides an explicit legal power for policy direction to the Canadian Transport Commission, the desirability of having policy statements issued by the government has been recognized by the Commission itself. As the President of the CTC, the Hon. Edgar Benson, told the Committee, "the Air Transport Committee, acting for the Commission, has been responsive to relevant government policy statements." (49:7)

Chapter 4

THE TRANSPORT CANADA POLICY PAPER

In February 1981, Transport Canada published the results of extensive studies on domestic air transportation in a report entitled "Economic Regulation and Competition in the Domestic Air Carrier Industry". Six months later, in August 1981, Transport Canada issued its "Proposed Domestic Air Carrier Policy (Unit Toll)", which was distributed for comments and discussion to all interested parties and which formed the central document in the Committee's proceedings.

Transport Canada gave the following reasons for proposing a new domestic air carrier policy at this time:

Since the mid-1970s, the evolution of the domestic air carrier industry has created a growing need to re-examine the federal government's policies defining (explicitly and by implication) the kinds of domestic routes that should be served by the National, Regional and Local carriers. The resulting uncertainty about the "roles" of the three main groups of carriers has created difficulties for the Canadian Transport Commission in the exercise of its licensing responsibilities, and has handicapped the carriers themselves in their planning by creating uncertainty about the sorts of routes for which they and others might reasonably expect to be licensed. (page 1 of the policy paper)

The objectives set out in the policy paper are presented and discussed in Chapter 6. Under the proposal, the regulatory function of the CTC would not change, and all carriers would be required to obtain CTC approval for:

- new routes and route abandonment;
- changes in operating restrictions (e.g., frequency of flights, size of aircraft, etc.);

—fare changes; and

—acquisitions and mergers.

The policy paper proposes specific roles for all domestic unit toll air carriers that correspond closely to the *de facto* roles of the carriers. To ensure that these distinct roles are maintained, various restrictions would be imposed on the types of services that air carriers could operate. These restrictions (with some exceptions permitted in unusual circumstances) are as follows:

—Air Canada and CP Air would continue to be the only two national carriers;

—the two national carriers would be restricted to the use of Group F and larger aircraft, and could not establish new services to northern Canada (north of 60° N latitude);

—EPA, Quebecair, Nordair and PWA would continue to be the only regional carriers;

—PWA would be confined to routes west of a line running between Winnipeg and Resolute Bay, and the three eastern regionals would be restricted to routes east of this line;

—in southern Canada, the regional carriers could operate non-stop flights of no greater than 800 miles; and

—local air carriers would be restricted to using non-jet aircraft for passenger flights in southern Canada.

Chapter 5

THE QUESTION OF DEREGULATION

The Committee noted that the Transport Canada policy paper postulates that the airline industry is going to continue to operate in a regulated environment.

In view of the recommendations made by several parties and also in view of the widespread interest created in Canada by the United States decision to deregulate its airline industry in 1978, the Committee did not think that this postulate could be taken for granted.

Arguments Favouring Deregulation in Canada

The Committee heard from a number of witnesses advocating varying degrees of reduction of government intervention in the industry. Chief among these were the Economic Council of Canada, the Bureau of Competition Policy in the Department of Consumer & Corporate Affairs, the Consumers' Association of Canada and several academics.

The Economic Council of Canada, in its criticism of the Transport Canada paper, claimed:

What distinguishes carriers operating in a fully competitive system from those operating under the Domestic Air Carrier Policy Proposals is their much greater flexibility to move in and out of given routes, to modify the type and level of airline service they are providing, and to adjust their equipment as they see fit. Such flexibility is essential if Canadians are to reap the full benefits that go with a highly dynamic and efficient airline industry. (40:66)

Reiterating the recommendations made in their report to the First Ministers arising from the Regulation Reference, the Economic Council advocated a phased transition, over a period of five years, to free entry on all routes. During the transition phase, small carriers would be able to compete with the regionals, regionals with each other and with the nationals, and the two nationals with each other, on all routes. After five years, the larger carriers would be able to compete with smaller carriers on routes previously reserved for them. The regulatory role of the CTC would also be terminated.

A similar approach was endorsed by Mr. Lawson Hunter, Director of Investigation and Research and Assistant Deputy Minister, Bureau of Competition Policy. He criticized the Transport Canada policy paper for failing to consider explicitly the interests of airline passengers, who have responded favourably to cheaper fares, lower levels of service, off-peak pricing, and other pricing and service options made available in Canada and the United States in recent years. Free entry—the end of regulated competition—would, in Mr. Hunter's opinion, stimulate "higher load factors, greater plane utilization and increased seating densities, thus improving efficiency and reducing costs". (40:40) He urged that "optimal carrier performance, not system stability, be the proper focus of [the Committee's] deliberations". (40:37)

More generally, the proponents of deregulation argued that regulation represented a net burden on consumers and that present policies were a major impediment to achieving optimal performance in the industry. Several arguments were presented to the Committee:

- 1) The airline industry is no longer an infant industry and the rationale for economic regulation has disappeared. The industry is not a natural monopoly, nor is it subject to significant economies of scale. The wide diversity of aircraft permits small carriers to operate efficiently on routes where larger carriers could not. The public treats airlines as the normal means of long distance travel, and there is no need for the government to promote it. Finally, while the air industry as a whole is important to the country, there is no economic reason to treat it as a public utility.
- 2) New entrants have a lower cost structure than existing carriers. They are more specialized, and have lower salary scales and higher personnel productivity. Given relaxed rules of entry, new competitors could find "simple highly specialized networks over relatively dense, short haul city-pairs" and "provide safe reliable service at much lower prices than presently exist". (Baldwin, 51:24)
- 3) In a deregulated environment, the threat of competition posed by free carrier entry acts as a continuous and powerful stimulus to carrier efficiency, innovation and service quality.

In criticizing the market dominance that currently exists in Canada, where Air Canada and CP Air account for about 80 per cent of the market, those who favour deregulation argued that such a situation cannot be defended on the grounds of efficiency. At the same

time, some observers had concerns about the preponderance of Air Canada and how a competitive market could work with one carrier having so large a market share.

Furthermore, the involvement of federal and provincial governments in many airlines was a source of concern to the proponents of deregulation, who argued that these carriers have access to lower cost financing than do privately owned carriers. Whether Crown ownership was compatible with a deregulated environment was an issue that needed attention, in the view of some experts.

For this reason, the Consumers' Association of Canada called for the privatization of Air Canada, and the Economic Council, in its report arising from the Regulation Reference, called for the termination of all support by governments of Crown-owned airlines.

It was noted also that the apprehended loss of services by small communities in the U.S. had not materialized and that subsidies for continuing service provided for by the *Airline Deregulation Act* of 1978 had been used only to a very small extent.

Arguments Opposing Deregulation in Canada

The Committee also heard the views of those who favour the maintenance of regulation in the airline industry. Their general philosophy is well represented by the following statements. In its brief, the Council of Unions in the Aviation Industry of the Canadian Labour Congress declared:

Air Transportation is an important public utility, with a crucial social and economic role, particularly in a vast, sparsely populated country like Canada. The random play of market forces simply cannot take adequate account of these social and economic needs.

One of the American experts, Mr. Melvin Brenner, said:

I submit that part of the issue which must be considered here is that an air transport system, a total and reasonably balanced system, is important in the national interest. This was the view we had in the States and within a framework of regulation. The whole purpose of regulation was to try to preserve a total network with reasonable balance. That has, at the very least, diminished with deregulation. (48:56)

The arguments of the opponents of deregulation were in general articulated around the following points:

- 1) The system of airline regulation in Canada has not produced an inefficient industry. It has permitted airlines to offer inexpensive and efficient services in an

environment of increasing competition. For the past several years, various decisions by the CTC and the Minister of Transport have expanded the range of operations of many carriers and have allowed for the introduction of low-cost unit toll and charter fares. There is no evidence that, under regulation, Canadian airlines have been earning excessively high returns on investment.

- 2) Canada and the United States have fundamentally different route structures and population densities. The top three routes in Canada in terms of traffic volume would be 5th, 17th and 62nd respectively if they were in the United States.

Moreover, the generally linear pattern of Canadian traffic flows would not allow, without wasteful duplication of services, the multiplication of the number of services and carriers that the denser hub and spoke patterns of air traffic permit in the United States.

Finally, many remote Canadian areas have no means of transportation other than air service, contrary to the United States, where surface modes are more widely available. Excessive competition would jeopardize the existence of these, and this would create more serious problems in Canada than in the United States.

- 3) The air transportation system must be considered a public utility, and stability must be one of its prime characteristics. This cannot be achieved under deregulation by relying only on free market forces.

The Committee's Views

The Committee shares the concern of those who are searching for ways to improve the overall efficiency of the airline industry and agrees that increased competition should be the preferred instrument for bringing this about. The Committee does not believe, however, that deregulation should be approached on a 'take it or leave it' basis.

The Committee has noticed that the performance of the industry in Canada has been relatively satisfactory in terms of public convenience, price levels, service stability and airline viability. The inadequacy of returns on investment, which is real in the view of the Committee, has not been linked convincingly to the existence of regulation.

The Committee was impressed with certain benefits that have resulted from the high level of competition that exists in the American airline industry, such as the provision of low-cost specialized services. However, the Committee has reservations about wholesale adoption of the American approach. Because of the dissimilarities between Canada and the United States, the Committee is not persuaded that transplanting the U.S. experiment would prove beneficial to this country. The balance of benefits of full deregulation cannot yet be ascertained, and the troubled state of the U.S. airline industry suggests caution in emulating

that example. Record high interest rates, rapidly rising fuel prices and the decline of the economy contributed greatly to the present predicament of the industry and complicated the analysis of the effects of deregulation.

It is evident, however, that deregulation has played some part in exacerbating the economic troubles of the airline industry, described by Mr. Roy Pulsifer as "the worst decline in its history". (48:7) The industry in the United States is suffering from severe problems of over-capacity and under-pricing on certain routes, and several large firms are near bankruptcy because of inappropriate responses to the deregulated environment.

Furthermore, there is no evidence that deregulation has created an overall lowering of air fares in the United States. On certain high density routes, rates have dropped, but on less competitive routes they have risen considerably. Overall, rates have risen by 17 per cent per annum since deregulation. (48:14)

Finally, the Committee holds the view that the stability of the air transportation system in Canada is an important goal that cannot be pursued through total deregulation.

In the light of this analysis, **the Committee has concluded that a regulated environment should be maintained for the domestic air industry and that the Canadian Transport Commission should continue to be the regulator.** At the same time, the Committee is persuaded that the prospect of competition is the principal inducement to efficient performance in the airline industry. Accordingly, the Committee will, in subsequent chapters of this report, advocate a régime that should increase competition within a regulated environment.

Chapter 6

POLICY OBJECTIVES

The policy objectives of Transport Canada's paper are described as follows (paragraph 38):

A new policy defining the roles of the domestic unit toll air carriers should:

- 1) provide an environment that promotes:
 - (a) adequate, stable air service to all parts of Canada where unit toll services are warranted by travel demand, with little need for direct operating subsidies;
 - (b) air carrier innovation and efficiency;
 - (c) industry financial stability; and
 - (d) reasonable opportunities for access to additional points for all carriers;
- 2) respect existing carrier rights and licence authorities to the greatest possible extent;
- 3) provide guidance to the Canadian Transport Commission without imposing a rigid structure on its consideration of whether a proposed service "is and will be required by the present and future public convenience and necessity."

The Committee considers that these objectives have certain weaknesses:

- they place too much emphasis on the determination of air carrier roles as the instrument of policy;

—they are overly protective of individual air carriers;

—while their attention to the adequacy and stability of air services in remote and less populated areas is justified, these attributes of services should have less importance in more developed parts of the country;

—they place too little emphasis on increasing the efficiency of the air transport system as a whole; and

—they fail to give any attention to what is important to consumers—the quality, cost and variety of the air services provided.

In view of these deficiencies, the Committee believes that the pursuit of these objectives would not produce the kind of air transport system that is needed in Canada. The Committee would prefer a set of objectives that places more emphasis on the overall efficiency of the system, including both carriers and infrastructure, and makes it clear that the prime beneficiary of the policy is the travelling public.

The Committee therefore recommends that the following objectives be stated in the future domestic air carrier policy. **A new domestic unit toll air carrier policy should promote:**

—**increased efficiency of the air transportation system;**

—**improved passenger convenience;**

—**the provision of an adequate choice of air services and fares;**

—**the long-term financial viability of the industry; and**

—**adequate and stable services in remote and less populated areas of the country.**

Chapter 7

AIR CARRIER ROLES

The control of market entry is accomplished in two stages. The first is constituted by government policy, which describes in general terms which types of carrier should be allowed to do what. The second is the test of public convenience and necessity administered by the CTC on applications filed by carriers.

The most commonly used mechanism at the first stage is the definition of roles for each group of carriers and the assignment of physical limits within which each group may conduct operations. This approach is followed in the Transport Canada policy paper and is summarized in Chapter 4 of this report. The rationale given for establishing clearly defined roles for air carriers is given in paragraph 39 of the proposed policy:

It was assumed that an evolutionary development of the industry is desirable and that a statement of the carriers' roles at this time would contribute to such development, by allowing the carriers to plan better by knowing the parameters of their potential operations within a regulated environment. Conversely, it was assumed that abolishing the concept of roles for different groups of carriers at this time would be unduly disruptive.

Testimony Before The Committee

Air Carriers

Canadian airlines that now provide unit toll services generally support the notion of roles for domestic air carriers. They all disagree, however, on what those roles should be. Not surprisingly, their objections largely reflect their individual interests.

Air Canada and CP Air generally favoured the proposed roles, but wanted tougher restrictions on the operations of regional carriers than those proposed and, further, did not want to be restricted themselves from operating in northern Canada or operating aircraft smaller than Group F (Boeing 737-size aircraft).

All of the regionals wanted to see the role of the national carriers confined to the longer haul routes and wanted the nationals—particularly Air Canada—to give up some of the short haul routes that they now serve.

Only EPA was satisfied with the proposed dividing line at Winnipeg. PWA wanted the line moved to Toronto, Quebecair wanted to have it at Calgary, and Nordair wanted to retain the four regions specified in the Regional Air Carrier policy statements of 1966 and 1969. Nordair was the only regional that did not oppose the proposed 800-mile limit on non-stop flights in southern Canada.

Among the nationals and regionals, only CP Air argued against restricting local carriers to non-jets. Air Canada, Nordair and Quebecair argued for tougher restrictions on operations by local air carriers than those contained in the proposed policy.

The local carriers appeared to favour strongly the maintenance of limited competition through continued regulation, but opposed the restriction that would prevent them from using jet aircraft in southern Canada. Local carriers have long sought the establishment of a policy that would acknowledge their existence and identify their role.

Wardair proposed that it should become a third national carrier.

Provincial and Territorial Governments

Seven provincial governments and the two territories expressed a range of views on the proposed air carrier roles.* Saskatchewan was the most supportive, objecting only to the provisions that would bar locals from using jets in southern Canada and prevent the nationals from applying to provide services in northern Canada. The Northwest Territories and Yukon shared these two objections, but also wanted consideration given to the designation of another carrier as the regional carrier for northern Canada. In addition, Yukon believed that there may be room for another regional carrier in western Canada. Prince Edward Island's principal objection was to the 800-mile limit on non-stop flights by regional carriers. New Brunswick wanted the operations of local carriers restricted by a maximum distance limit and did not want the nationals barred from using smaller jet equipment.

* All provinces and both territories were invited to appear before the Committee. Manitoba, Ontario and Saskatchewan did so; New Brunswick, Newfoundland, Nova Scotia, Prince Edward Island and the two territories made written submissions.

Manitoba wanted the east-west dividing line moved to Toronto, because the proposed line through Winnipeg would prevent PWA from connecting points west of Winnipeg with communities in northeast Manitoba. Manitoba also suggested that the local carriers be divided into two groups, the larger being designated as sub-regional carriers, and that the northern boundary for the nationals be the Precambrian Shield rather than the 60th parallel.

Newfoundland and Ontario expressed views that were highly critical of the proposed policy. Newfoundland expressed its reservations as follows (page 2 of the submission):

We do not, however, believe that it is necessary to restrict the number of carriers in specific roles, limit the non-stop distance on Regional routes, nor restrict Local carriers to non-jet equipment. If the industry is to evolve as suggested, it must be permitted to do so on the basis of market demand.

Although Ontario favoured continued regulation, it proposed (page 5 of the submission) "a much less restrictive policy which defines the primary functions of each of the three types of carriers, but does not necessarily preclude them from offering other services". Ontario specifically opposed: restricting the numbers of national and regional carriers to two and four respectively; establishing boundaries for regionals; limiting non-stop flights by regionals to 800 miles; preventing locals from using jets and nationals from using turbo-props; and disallowing Wardair and other charter carriers from providing unit toll services. Although Ontario believed that regional air carriers should "be permitted to develop within each of the economic regions of Canada" (page 16 of the submission), it wanted any carrier, new or old, to be able to apply to the CTC to operate any unit toll service in Canada.

Other Witnesses

Most other witnesses who appeared before the Committee opposed the establishment of roles for domestic unit toll carriers. Some held this view because they favoured an eventual elimination of all economic regulation of the airline industry, others because they believed that government policy statements should not restrict the Canadian Transport Commission from considering all applications on a case-by-case basis.

The Alliance of Canadian Travel Associations and the Council of Unions in the Aviation Industry (of the Canadian Labour Congress) did not comment directly on the matter of carrier roles, but generally believed that the proposed policy is too inflexible. The Council expressed its view as follows (page 5 of the submission):

We would be better served by an air transport policy which was based on clearer principles and allowed greater structural flexibility. Flexibility is particularly crucial in an industry like air transport in which even the short- and medium-term outlook is difficult to forecast.

The Committee's Views on the Transport Canada Paper

Flexibility

The Committee is generally satisfied with the way domestic air transportation has changed over the past few years and would like to see this evolution continue. For it to continue, however, the policy must be at least as flexible as the *de facto* policy framework that exists now. Any future policy should permit, as warranted by market demand, a greater degree of competition and allow greater flexibility for air carriers to adapt to changing circumstances.

It is the view of the Committee that the air carrier roles proposed by Transport Canada are too restrictive to permit the efficient development of the air carrier industry in the years to come. In a sense, the proposed roles are more restrictive than even the present situation, in that regional air carriers are not now prevented by policy from applying for routes that cross the proposed dividing line at Winnipeg or to operate non-stop flights exceeding 800 miles, and local air carriers can apply to acquire jet aircraft for use on routes of any length.

The Committee is convinced that any rigid barriers defining the roles of air carriers would seriously impede the efficient development of the industry and would deny the travelling public the most desirable choices of services and fares. The air transport system is so complex and the future is so uncertain that it is simply not possible to set out a complex set of constraints that could be expected to guide the industry in the right direction over the next several years. Air carriers need more elbow room to manage their enterprises in the most efficient manner possible and to be in a position to respond to new opportunities and changing circumstances.

Competition

The Committee is concerned by the fact that the policy paper does not allow new entrants at the national and regional levels. Although there is an argument for limiting to two the number of national carriers, the Committee regards competition—and the threat of it—as essential to the achievement of the policy objectives that it has set out in Chapter 6 of this report. Accordingly, the Committee believes, in principle, that market entry should not be restricted by physical criteria set out in government policy.

Neither should the policy prevent local carriers and newly established carriers from competing head-on with the national and regional carriers. There may well be routes in Canada where efficiency or service could be improved by allowing a local or a newly established carrier to compete directly with a regional or national carrier. The regional carriers likewise should not be restricted from offering worthwhile services that they could best provide and that would allow them to improve the utilisation of their present equipment.

The Committee believes that it would be much better for the CTC to consider applications case by case rather than have applications ruled out by rigid roles. Not only would this less restrictive approach allow for the introduction of potentially worthwhile new services, but the threat of market entry would provide an additional incentive for the national and regional carriers to operate efficiently and charge competitive fares.

Air Carrier Planning

It has been claimed that an important benefit of establishing carrier roles is that it allows carriers to plan better for the future. It is argued that by defining the types of services that air carriers are allowed to provide, all carriers would be able to gauge better the type and amount of competition that they would face in the future and thereby reduce their investment risk. The Committee believes, however, that this reduction in risk may come at a price. The reduced flexibility that carriers have with a tight role definition could make it difficult for them to use their resources in the most efficient manner possible and therefore to achieve maximum benefit from their investment. Overall, it may well be that the costs of this reduced flexibility are much greater than the benefits of reduced risk.

Effect of Appeals

There is also a practical objection to the establishment of rigid carrier roles. Soon after its adoption, the policy might be made obsolete as a result of a successful appeal that stood in direct conflict with the stated roles of the carriers. The Committee believes that it would be only a matter of time before common sense or political expediency would cause the Minister of Transport or the Governor in Council to uphold an appeal that was in direct conflict with any complex and rigid carrier roles defined in the policy.

Roles and Policy Guidance

The Committee recognizes that probably the clearest way of providing guidance to the CTC would be for the government to define carrier roles using detailed physical criteria. The Committee is concerned, however, that the price to be paid for such clarity is to accept a policy that lacks flexibility and impedes change. A definition of roles that is overly restrictive could pre-empt a carrier from demonstrating that a proposed service is justified by public convenience and necessity.

The Committee's Recommendations

Two-stage systems of entry regulation such as Canada now has can only work if the first stage—government policy—is less restrictive than the second stage—the review of an application by the CTC. The Committee believes that the approach advocated by Transport

Canada does not meet this test; it sees a danger that the Department's proposal would result in some worthwhile services being discouraged and others being approved as 'exceptional cases'. Over time, both these situations would undermine the policy.

Despite its conclusion that, in principle, air carrier roles should not be defined *a priori* by policy, the Committee has decided to recommend that, for the present, only Air Canada and CP Air be permitted to operate long haul, unit toll services in southern Canada (south of 60° N latitude). With this one exception, the Committee opposes the establishment of any restrictions that would limit the opportunities of any carriers, including new entrants, from applying to provide unit toll services anywhere in Canada, using any type of equipment. Every carrier should be allowed to make its case before the CTC for any proposed new service that does not conflict with this role definition for the national carriers.

There are two principal reasons for treating long haul routes differently from other routes. First, even with the limitation on the number of national carriers, Air Canada and CP Air would undoubtedly face a substantial increase in competition. They would be exposed to more competition from local and regional carriers on short and medium haul routes and, to some extent, from multi-stop services on long haul routes. They would also be competing more with each other and would continue to face stiff competition on trans-border and international routes. Furthermore, while the local and regional carriers (and any new entrant) would have much greater opportunities for expansion than they now have, the two national carriers would find relatively few new markets into which they could expand. Exposing the national carriers to even more competition by permitting other carriers to operate long haul routes would put at risk the extensive services that Air Canada and CP Air now operate, domestically as well as internationally.

Secondly, the Committee is concerned that if there is no limit on the number of national carriers permitted, local and regional carriers may become distracted from their primary responsibilities—providing good regional and local air services.

The Committee believes that limiting the number of national carriers to two is further justified by the fact that Air Canada and CP Air already provide convenient and frequent long haul services, complemented during busy periods by charter flights (ABCs) operated by other carriers. This competition has produced a variety of fare levels that adequately serve the needs of the travelling public, particularly at the low end of the fare scale.

Moreover, there are a relatively small number of long haul routes that can support non-stop flights. These routes account for only about 10 per cent of the total unit toll domestic traffic.

Having decided that long haul unit toll routes in southern Canada should, for the present, be reserved for Air Canada and CP Air, the Committee has to consider how long haul routes should be defined. The Committee believes that the limitation should not be

based on size or type of aircraft, for this could preclude carriers from using the most efficient aircraft. Neither does the Committee believe that the policy objectives would be well served by confining certain carriers to particular regions of the country. The only acceptable criterion would be to impose a maximum stage length restriction on all carriers other than the nationals. Furthermore, the distance chosen should be consistent with the efficient operation of the principal aircraft used by the regional carriers, the Boeing 737. The Committee recommends a distance of 1500 (great circle) statute miles, the approximate range of this aircraft. By way of example, only Air Canada and CP Air would be able to operate Toronto-Calgary, Toronto-Edmonton or Toronto-Vancouver with non-stop flights. On the other hand, any carrier could apply to serve such routes as St. John's-Toronto, Vancouver-Regina-Toronto or Toronto-Winnipeg-Calgary.

In summary, the Committee makes the following recommendations concerning air carrier roles.

In southern Canada (south of 60° N latitude), only Air Canada and CP Air should be allowed to operate unit toll services between city-pairs more than 1500 great circle statute miles apart.

Any Canadian air carrier, new or existing, should be able to apply to the CTC to operate any unit toll service in southern Canada between city-pairs up to 1500 miles apart.

Any Canadian air carrier, new or existing, should be permitted to apply to the CTC to operate any domestic unit toll service to or within northern Canada (north of 60° N latitude).

No restrictions should be laid down in policy on the size or type of aircraft that domestic unit toll carriers may operate.

Effects of the Proposed Roles

On short and medium haul routes, the increased threat of entry would stimulate carrier efficiency and service. On long haul routes, the potential threat of competition from other carriers' multi-stop services would have the same effect and, in addition, should result in more long haul, non-stop services being offered by national carriers than would be the case if this threat did not exist.

The current weakness in the economy and the limited traffic growth expected in the short to medium term should prompt the CTC to exercise care in increasing competition among the carriers too quickly. In the long run, however, the minimum role definition that the Committee is proposing should promote the objectives set forth in this proposed policy. A

redistribution of market shares would take place, fleet planning strategies would be re-oriented, weaker carriers might be merged with more efficient ones, and new low-cost carriers might emerge. The proposed roles provide the flexibility that is necessary for this process of change to continue and to produce a stronger air carrier industry that provides good service at a fair price.

The Role of Air Canada

The Committee heard a wide variety of views concerning Air Canada, ranging from the opinion that a strong Air Canada is needed as a tool of government policy to the wish that Air Canada be reduced in size and sold to private investors. The proponents of the latter view argued that it is not possible for fair competition to occur as long as Air Canada continues to dominate the marketplace and have access to cheaper capital than is available to privately owned carriers.

The Committee recognizes that Air Canada's predominance and public ownership may be a legitimate cause for concern. It is evident, however, that Air Canada has not made unfair use of its strength in competition with other carriers. The Committee also noted that between 1977 and 1981, the percentage of all domestic passengers that were carried by Air Canada declined from 56 to 48 per cent.

The Committee proposes no change in Air Canada's role or status at this time.

Domestic Charters

The matter of domestic Advance Booking Charters (ABCs) was brought up during the hearings and was also mentioned in the Transport Canada proposed policy. The main issue raised before the Committee is whether the distinction that now exists between ABCs and unit toll services should be maintained.

This distinction currently exists on two levels:

- the two types of services are operated under different classes of licences—mainly Class 1 for unit toll services and Class 4 for charter services; and
- the rules under which ABCs operate are aimed at those leisure travellers who are willing to forgo flexibility in favour of low price.

The range of views expressed on this matter is represented by the statements of Air Canada and Wardair. In its brief, Air Canada stated:

A real distinction must be maintained between unit toll and specialized charter services for leisure travel. Policy should state specifically that advance purchase and minimum stay requirements be no less stringent than at present. (page 4 of the submission)

Mr. Max Ward commented:

I do not really think that the proponents of this policy could possibly not recognize that the distinction between chartered and scheduled service has disappeared. (46:9)

Furthermore, the President of the CTC told the Committee that the CTC needs policy guidance to clarify the relationship between unit toll and charter services.

The Committee has noted that:

- if the fences around charter operations were lowered too far, the charter carriers would have a back door into unit toll services, without having to meet the obligations associated with unit toll licences;
- the present fences on ABCs, pertaining to advance booking and minimum stay requirements, are close to what the CTC study, "Assessment of the Effectiveness of the Restrictions on Low Priced Air Fares", considers optimum for domestic markets, i.e., "... a minimum stay requirement of three days with advance booking of 14 days . . ."; and
- domestic ABCs represent a very small fraction of the total operations of those carriers that have offered this service (about 5 per cent for Wardair and even less for the regional carriers).

These observations led the Committee to conclude that the distinction between unit toll and charter services should be maintained and that, because of the small size and specialized nature of domestic charter markets, this should not create any particular hardship for the charter carriers.

The Committee cannot ignore, however, that the existence of ABCs has been a very important factor in the development of the low fares now offered by the unit toll carriers.

For this reason, the Committee believes that it is important that domestic ABCs continue to be offered. To this end, the assertion by Mr. Max Ward that "the scheduled carriers can come out with low fares that we cannot possibly compete on" (46:8) must be taken seriously.

The Committee recognizes the potential ability of scheduled carriers to engage in predatory pricing by cross-subsidizing their low fares with their higher fares. By contrast, the opportunity for cross-subsidization by charter carriers is quite limited under the existing rules.

The Committee believes that while charter carriers should direct their services primarily toward the cost-conscious, discretionary market, they should be given greater access to higher yield markets, in order to improve their loads and yields. This seems to be the intent of the 'top-off' authority now contained in the Air Carrier Regulations, which allows up to one-third of the capacity of the aircraft to be sold without any pre-booking requirement. The Committee believes, however, that the other 'top-off' restrictions (i.e., round-trip obligation and minimum stay requirement) are an impediment to charter carriers who want to optimize their yields and load factors.

The Committee therefore recommends that these restrictions be relaxed so that charter carriers can compete more equitably in low-cost markets with scheduled carriers while at the same time having some access to higher yield markets.

In view of these considerations, the Committee recommends that restrictions on domestic charter services should be further reduced, but a distinction should be maintained between charter and unit toll services. Particular consideration should be given to eliminating the length of stay requirement and to allowing one-way trips for the one-third 'top-off' now permitted on ABC flights.

Subsidies

The Transport Canada policy paper is nearly silent on the question of whether direct operating subsidies should be paid to air carriers. It states only that the policy should promote unit toll air services that are "... warranted by travel demand, with little need for direct operating subsidies". (paragraph 38) Despite this lack of emphasis on subsidies, some witnesses argued before the Committee that in some instances, direct operating subsidies should be provided and that the position of the government toward the use of subsidies should be spelled out in the domestic air carrier policy.

Air services should be determined principally by the demand for such services, although operating subsidies may be required in order to initiate or maintain services that are essential to the public interest. Such subsidies, which would be administered by the CTC, should be granted for limited periods of time. They should go to the most appropriate carrier operating the most suitable equipment. In some instances, improvements in airports or air navigation services could be an alternative to granting operating subsidies.

The Committee wishes to note also that the provision of air carrier subsidies is not exclusively a federal responsibility. Ontario, for example, has been extremely successful in improving air services in northwestern Ontario through the Norontair operation, which it funds. This may be an area where the provinces might take on greater responsibility.

Transport Canada should undertake a detailed analysis of the matter of subsidies for air transportation. The report emanating from this study should be referred to this Committee.

Inter-carrier Co-operation

The effect of the Committee's recommendations would be to stimulate competition among Canada's domestic carriers. This competition should take place in the areas of prices and quality and convenience of services. There are areas, however, where carriers should co-operate for the benefit of the travelling public. These areas of co-operation include reservations and ticketing, joint fares and rates, and shared facilities and services.

The CTC has no powers in these areas. A longstanding legislative precedent in the *Railway Act* obliges railways and telephone companies to interconnect and forward each other's traffic on reasonable terms and conditions. Consumers and competitors may seek relief from the regulator if these obligations are not fulfilled.

The need for joint fares and the importance of electronic reservations systems suggest that an analogous legal obligation might apply to airlines. It would concern the terms of access to reservations systems and co-operation in ticketing and joint fares.

All carriers should co-operate through interline and inter-airline agreements in the areas of reservations and joint fares and rates. The CTC should investigate these issues, identify problems and recommend remedies.

Five-year Review

The Committee recognizes that the policy will have to be reviewed periodically. Changes in technology, market conditions and the structure of the industry may require modifications from time to time. In particular, as carriers adjust to an environment of increased competition, there may be room for more than two national carriers. **Transport Canada should issue a report within five years' time either reaffirming existing policy or proposing modifications. That report should be referred to this Committee for consideration.**

Chapter 8

POLICY GUIDANCE

In discharging its responsibilities, the CTC is guided by the *Aeronautics Act*, the *National Transportation Act* and government policy. Of these three sources of direction, the first two are necessarily paramount, because there is no legislative requirement for the CTC to take government policy into account in making its decisions. The provisions of these acts are, however, quite general and may be subject to varying interpretation. Moreover, the CTC has been responsive to government policy direction. From a practical point of view, therefore, government policy—expressed through policy statements and decisions on appeals—is likely to continue to have an important influence on CTC decisions. The Committee therefore attaches great importance to the general direction that might be given the CTC through government policy. Such guidance is particularly important in view of the Committee's recommendation that few constraints be placed on the opportunities open to carriers seeking CTC approval for new routes.

Control of Entry

The Committee's policy recommendations concerning market entry support a continuation of recent trends toward increased levels of competition. In reaching its decisions, the CTC should regard competition as the principal means by which the objectives of the policy will be promoted. Increased competition can be expected to result in increased efficiency and improvements in services and passenger convenience.

Although the Committee strongly supports a high level of competition among carriers, it wishes to express two caveats:

- Competition may be counterproductive if the entry of an additional competitor would fragment a market to a point where load factors were significantly reduced or carriers were forced to use smaller, less efficient aircraft.

—For sparsely populated remote areas, stability and adequacy of service should not be jeopardized by a level of competition that the market cannot sustain on a year-round basis.

In proposing a policy that would allow more competition, the Committee recognizes that some carriers may attempt to expand too quickly into new markets at the expense of their existing services. While air carriers should not be discouraged from experimentation and innovation, the CTC should ensure that the implementation of the policy proposed in this report does not create undue disruptions of existing services.

In light of these considerations, the Committee proposes that government policy provide the following direction to the CTC in respect of proposed new domestic unit toll air services.

Any air carrier, existing or newly established, could apply to the Canadian Transport Commission to provide unit toll passenger or cargo air services on any route in Canada, subject to the 1500-mile limit (in southern Canada) imposed on all air carriers other than Air Canada and CP Air.

The CTC should authorize any domestic unit toll air service that would, on balance, further the policy objectives set out in Chapter 6 of this report. To this end, the Commission should:

- 1) rely on competition as the principal means of promoting the objectives of the policy, particularly in respect of high density markets and in short haul markets in which air services face strong competition from surface modes of transportation;**
- 2) ensure that when an existing air carrier applies to provide a new service, the provision of the service would not have a significant adverse effect on the applicant's existing services; and**
- 3) take into account, in determining whether the proposed service would result in an overall increase in efficiency of the air transport system, the effect that a proposed service would have on the costs and services of all carriers affected, as well as on the costs of any improvements to airports and air navigation services that would be required.**

The Committee recognizes that the approach it favours would place greater demands on the CTC than would the Transport Canada proposal. The CTC probably would be faced with a greater number of applications for new services and its decisions would in general be more difficult. At first, there might be a rush of applications, but this would not be expected to persist. Carriers would recognize that they are still in a regulated environment and that it would not be in their long-term interest to propose overly rapid expansion. Furthermore, the CTC's rejection of unsupported applications would tend to cause carriers to become more selective in proposing new services.

Fares and Rates

Air carriers have frequently complained that the requirements for filing rates and tariffs with the CTC are unnecessarily burdensome. The need to justify each change, no matter how minor, has been especially criticized. The Committee believes that fares and rates should continue to be controlled by the CTC but favours a more flexible process.

The CTC should continue to regulate fares and rates. In order to simplify rate-setting and encourage competition, the CTC should define, and from time to time amend, a zone of flexibility within which carriers would be allowed to vary their fares upward or downward with no other requirement than a short advance notice to the CTC.

The Committee expressed in Chapter 7 its concern that a competitive balance be maintained between ABCs and low-cost unit toll fares. To that effect, the Committee believes that the CTC should monitor closely low-cost fares filed by scheduled carriers and their associated fences. Low-cost fares could be defined as fares discounted from regular fares by more than the limit prescribed in the zone of flexibility defined in the previous recommendation. **The CTC should ensure that fair competition is maintained between ABCs and low-cost fares offered by scheduled carriers.**

Furthermore, scheduled carriers should be discouraged from offering deceptively small numbers of seats on highly publicized deep-discount fare schemes. **The Air Carrier Regulations should be amended to include a provision requiring scheduled carriers to state clearly in their advertisements for low-cost fares the number of seats allocated to these fares on each route.**

Mergers and Acquisitions

The Committee recognizes that mergers and acquisitions may at times be necessary to bring about structural changes in the industry that result in improved efficiency. The CTC must consider these changes on a case-by-case basis, weighing improvements in efficiency against the potential for reduced competition.

Mergers and acquisitions should be dealt with by the CTC case by case within the framework of the policy. The CTC should look favourably on proposed mergers and acquisitions that would result in improved efficiency, provided they would not unduly restrict competition.

Regulatory Burden

The burden of the regulatory process was referred to by several witnesses, including regional and local carriers and some provinces. Also, a Transport Canada survey of airline attitudes to regulation showed that air carriers were in wide agreement that the direct and indirect cost of regulation is too high.

The Committee was pleased to hear from the Hon. Edgar Benson, President of the CTC, and Mr. Malcolm Armstrong, Chairman of the Air Transport Committee, that the ATC is currently attempting to find ways of streamlining certain requirements imposed on air carriers, including those involving route applications and the filing of tariffs.

The CTC should give high priority to simplifying and speeding up its procedures in order to reduce the regulatory burden on the air carriers. In particular, the CTC should:

- establish time limits for its consideration of different types of applications;
- expedite unopposed licence applications;
- simplify the processing of applications for upgrading the aircraft group on existing licences for smaller aircraft (Groups A to C); and
- simplify the process of filing domestic charter programs so that the requirements are no more burdensome than those for filing competing low-cost, unit toll fares.

Appeals

The ultimate responsibility for policy guidance rests with the government, and the appeal process is an important means to review the manner in which policy has been applied by the CTC in particular cases.

The Committee notes the concern of Transport Canada that the increasing tendency to appeal CTC decisions is placing a growing burden on the government.

The enunciation of clear government policy with respect to domestic air carrier operations will in itself diminish the number of appeals. Furthermore, the Committee considers that the Minister and the Cabinet, by establishing the basis on which appeals will be heard, could reduce the number of appeals.

Both the Minister and the Cabinet have broad discretion with respect to appeals from CTC decisions. A clarification of how that discretion will be exercised through the publication of guidelines for appeals from CTC decisions—in effect, an appeals policy—would be an appropriate and positive addition to the regulatory process.

The Committee considers that appeals from decisions of the CTC should be retained. To limit the number of appeals, the Minister and the Governor in Council should establish and make public the basis upon which appeals would be heard.

Chapter 9

SUMMARY OF RECOMMENDATIONS

The Standing Committee on Transport makes the following recommendations:

Regulation

1. A regulated environment should be maintained for the domestic air industry, and the Canadian Transport Commission should continue to be the regulator. (21)*

Policy Objectives

2. The objectives of a new domestic unit toll air carrier policy should be to promote:
 - increased efficiency of the air transportation system;
 - improved passenger convenience;
 - the provision of an adequate choice of air services and fares;
 - the long-term financial viability of the industry; and
 - adequate and stable services in remote and less populated areas of the country. (24)

* Recommendations can be found in the text on the pages indicated in parentheses.

Air Carrier Roles

- 3. In southern Canada (south of 60° N latitude), only Air Canada and CP Air should be allowed to operate unit toll services between city-pairs more than 1500 great circle statute miles apart. (31)**
- 4. Any Canadian air carrier, new or existing, should be able to apply to the CTC to operate any unit toll service in southern Canada between city-pairs up to 1500 miles apart. (31)**
- 5. Any Canadian air carrier, new or existing, should be permitted to apply to the CTC to operate any domestic unit toll service to or within northern Canada (north of 60° N latitude). (31)**
- 6. No restrictions should be laid down in policy on the size or type of aircraft that domestic unit toll carriers may operate. (31)**

Domestic Charters

- 7. Restrictions on domestic charter services should be further reduced, but a distinction should be maintained between charter and unit toll services. Particular consideration should be given to eliminating the length of stay requirement and to allowing one-way trips for the one-third 'top-off' now permitted on ABC flights. (34)**

New Entry

- 8. The CTC should authorize any new domestic unit toll air service that would, on balance, further the objectives set out in recommendation 2 and, in particular, should:**
 - a) rely on competition as the principal means of promoting the objectives, particularly in respect of high density markets and in short haul markets in which air services face strong competition from surface modes of transportation;**
 - b) ensure that when an existing air carrier applies to provide a new service, the provision of the service would not have significant adverse effect on the applicant's existing services; and**
 - c) take into account, in determining whether the proposed service would result in an overall increase in efficiency of the air transport system, the effect that a proposed service would have on the costs and services of all carriers affected, as well as on the costs of any improvements to airports and air navigation services that would be required. (38)**

- Fares and Rates
9. The CTC should continue to regulate fares and rates. In order to simplify rate-setting and encourage competition, the CTC should define and, from time to time, amend a zone of flexibility within which carriers would be allowed to vary their fares upward or downward with no requirement other than a short advance notice to the CTC. (39)
- Low-cost Fares
10. The CTC should ensure that fair competition is maintained between ABCs and low-cost fares offered by scheduled carriers. (39)
- Advertising of Low Fares
11. The Air Carrier Regulations should be amended to include a provision requiring scheduled carriers to state clearly in their advertisements for low-cost fares the number of seats being offered at those fares on each route. (39)
- Mergers and Acquisitions
12. Mergers and acquisitions should be dealt with by the CTC case by case within the framework of the policy. The CTC should look favourably on proposed mergers and acquisitions that would result in improved efficiency, provided they would not unduly restrict competition. (39)
- Regulatory Burden
13. The CTC should give high priority to simplifying and speeding up its procedures in order to reduce the regulatory burden on the air carriers. In particular, the CTC should:
- establish time limits for its consideration of different types of applications;
 - expedite unopposed licence applications;
 - simplify the processing of applications for upgrading the aircraft group on existing licences for smaller aircraft (Groups A to C); and
 - simplify the process of filing domestic charter programs so that the requirements are no more burdensome than those for filing competing low-cost, unit toll fares. (40)
- Air Carrier Subsidies
14. Air services should be determined principally by the demand for such services, although operating subsidies may be required in order to initiate or maintain services that are essential to the public interest. Such subsidies, which would be administered by the CTC, should be granted for limited periods of time. They should go to the most appropriate carrier operating the most suitable equipment. (34)
15. All carriers should co-operate through interline and inter-airline agreements in the areas of reservations and joint fares and rates. The CTC should investigate these issues, identify problems and recommend remedies. (35)

Appeals

16. Appeals from decisions of the CTC should be retained. To limit the number of appeals, the Minister and the Governor in Council should establish and make public the basis upon which appeals would be heard. (40)

Five-year Review

17. Transport Canada should issue a report within five years' time either reaffirming existing policy or proposing modifications. That report should be referred to this Committee for consideration. (35)

GLOSSARY

ABC: Advance Booking Charter. Chartered flights for which seats are sold through a tour operator and where passengers must comply with advance booking and minimum stay requirements.

Aircraft Groups: For licencing purposes, aircraft are divided into eight groups, according to maximum take-off weight.

<i>Group</i>	<i>Weight Range (lbs)</i>	<i>Types of Aircraft in Group</i>
A	up to 4,300	Cessna 180, 182, 185, 206
B	4,300 — 7,000	Cessna 310, 402, DH Beaver
C	7,000 — 18,000	DHC-6, Beech 99
D	18,000 — 35,000	DC-3
E	35,000 — 75,000	DHC-7, F-27, HS-748
F	75,000 — 150,000	B-737, DC-9, BAC-111, Electra
G	150,000 — 300,000	B-727, B-707, B-767, DC-8
H	300,000 and over	B-747, DC-10, L-1011

ATC: Air Transport Committee of the Canadian Transport Commission.

Charter Service: Air services in which an entire aircraft is chartered for a fee.

Class of Air Service: For licencing purposes, domestic air services are divided into classes. Classes 1, 2 and 3 are unit toll services (see **Unit Toll Services**), differentiated by the degree of regularity required of the service. Most national and regional carrier unit toll services are operated under Class 1 licences.

Conditions of Service: Restrictions attached to licences in respect of routes that air carriers are allowed to serve. These are most commonly mandatory stops, maximum service frequency and number of aircraft.

CTC: Canadian Transport Commission.

Fences: Restrictions on the sale of seats. Common types of fences are minimum pre-booking period, advance purchase of ticket, cancellation penalties and minimum length of stay.

Market Entry and Exit: The process of an air carrier initiating (**entry**) or terminating (**exit**) services on a particular route (**market**).

Unit Toll Services: Passenger services in which individual seats are sold to the public, or cargo services in which goods are shipped for a fee related to the type of commodity and the weight of the goods.

Yield: A measure of the average revenue produced per unit of passengers or cargo carried, usually expressed in dollars per passenger or per passenger-mile (kilometre) and dollars per pound (kilogram) or per ton-mile (kilometre) for cargo.

Appendix A

WITNESSES WHO APPEARED BEFORE THE COMMITTEE

Issue No.

Tuesday, February 2, 1982

Department of Transport,
Canadian Air Transportation Administration:

40

Mr. Richard P. St-John
Deputy Administrator

Mr. J.A.A. Lovink
Director
Domestic Policy (Air)

Department of Consumer and Corporate Affairs,
Bureau of Competition Policy:

40

Mr. Lawson Hunter
Director of Investigation and Research

Mr. D.A. Dawson
Director
Regulated Sector Branch

Dr. D.F. McKinley
Director
Research and International Relations Branch

Economic Council of Canada:

40

Mr. David W. Slater
Chairman

Mr. Robert Jenness
Senior Policy Advisor

Wednesday, February 3, 1982

Department of Transport,
Canadian Air Transportation Administration

41

Mr. J.A.A. Lovink
Director
Domestic Policy (Air)

Thursday, February 4, 1982

Pacific Western Airlines Limited: 42

Mr. Rhys R. Eyton
President and Chief Executive Officer

Eastern Provincial Airways Limited: 42

Mr. William Verrier
Vice-President, Marketing

Mr. Roy Rideout
Vice-President
Administration and Planning

Nordair: 42

Mr. Roland Lefrançois, Q.C.
Chairman of the Board

Quebecair: 43

Mr. Alfred Hamel
President and Chief Executive Officer

Tuesday, February 9, 1982

Time Air Limited: 44

Mr. Richard Barton
President

Bradley Air Services/First Air: 44

Mr. John W. Crichton
Executive Vice-President

Northwest Territorial Airways Limited: 44

Mr. Robert Engle
President

Canadian Pacific Air Line, Limited (CP Air): 45

Mr. Ian A. Gray
President and Chief Executive Officer

Thursday, February 11, 1982

Wardair Canada (1975) Ltd: 46

Mr. Maxwell Ward
Chairman and President

Air Canada: 46
Mr. Claude I. Taylor
President and Chief Executive Officer

Consumers' Association of Canada: 47
Mr. Hudson Janisch
Chairman, Regulated Industries Program and
Professor of Law, University of Toronto
Mr. John Blakney
Assistant Counsel

Air Chicago, Chicago, Illinois: 47
Mr. Brian Campbell
Chairman

Tuesday, February 16, 1982

Panel Discussion on Airline Deregulation in the United States: 48

Mr. Roy Pulsifer
Associate Director
Licensing Programs and Policy Development
Bureau of Domestic Aviation
Civil Aeronautics Board
Washington, D.C.

Mr. Melvin A. Brenner
Melvin A. Brenner Associates, Inc.
Rowayton, Connecticut

Mr. Dennis F.X. Mathaisel
Postdoctoral Research Associate and Lecturer
Flight Transportation Laboratory
Department of Aeronautics and Astronautics
Massachusetts Institute of Technology
Cambridge, Massachusetts

Mr. Robert J. Joedicke
Lehman Brothers Kuhn Loeb Research
New York, N.Y.

Alliance of Canadian Travel Associations: 48

Mr. Doug Crozier
Legal Counsel

Mr. Gareth Davies
Executive Director

Mr. Alex Bertren-Matthews
Vice-President

Thursday, February 18, 1982

Canadian Transport Commission:

The Honourable E.J. Benson
President

Mr. M.D. Armstrong
Chairman
Air Transport Committee

Mr. Richard Fosbrooke
Acting Director
Passenger & Aviation Economics

49

Province of Saskatchewan:

Mr. John S. Burton
Executive Director
Transportation Agency of Saskatchewan

49

Province of Manitoba:

The Honourable Samuel Uskiw
Minister of Highways and Transportation

Mr. John C. Rea
Director of Transportation
Department of Highways and Transportation

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Tuesday, February 23, 1982

Panel Discussion on Domestic Air Carrier Policy:

Dr. W.T. Stanbury
Professor of Policy Analysis
Faculty of Commerce
University of British Columbia and
Director, Regulation and Government
Intervention Program,
The Institute for Research on Public Policy

Mr. F.J.H. Johnston
Air Transport Director
Air Transport Department
International Air Transport Association
Montreal, Quebec

Mr. William A. Jordan
Professor of Economics
Faculty of Administrative Studies
York University
Downsview, Ontario

51

Mr. J.R. Baldwin
Associate Professor of Economics
Department of Economics
Queen's University
Kingston, Ontario

Province of Ontario:

Mr. W.D. Burtnick, Q.C.
Senior External Counsel
Office of Legal Services
Ministry of Transportation and Communications

Mr. David Garner
Air Office

51

Thursday, February 25, 1982

Dr. Richard Schultz
Associate Professor
Department of Political Science and
Centre for the Study of Regulated Industries
McGill University
Montreal, Quebec

52

Mr. J.M. Fugère
President
Pilgrim Airlines
New London, Connecticut

52

Institute for Transportation Studies,
University of Calgary:

53

Mr. Everett Johnston
Chairman

Mr. J.R. Brent Ritchie
Director
Division of Travel and Tourism

Tuesday, March 2, 1982

Council of Unions in the Aviation Industry,
Canadian Labour Congress:

54

Mr. Donald Montgomery
Chairman of the Council and
Secretary-Treasurer of the Congress

Mr. Murray Randall
National Representative
Canadian Labour Congress

Mr. Mike Rygus
General Vice-President
International Association of Machinists

Mr. Ron Schneiderman
Secretary-Treasurer
Canadian Air Line Dispatchers Association

Chairman
Air Transport Committee

Mr. Richard Postrooks
Assistant Director
Ministry of Aviation Economics

Province of Saskatchewan

Mr. John S. Burton
Executive Director
Transportation Agency of Saskatchewan

Province of Manitoba

The Honourable Samuel Uelef
Minister of Highways and Transportation
Mr. John C. Keel
Director of Transportation
Department of Highways and Transportation

Tuesday, February 23, 1981

Panel Discussion on Domestic Air Carrier Policy

Dr. W.T. Stanbury
Professor of Policy Analysis
Faculty of Commerce
University of British Columbia and
Director, Regulation and Government
Incentives Program,
The Institute for Research on Public Policy

Mr. F.J.H. Johnston
Air Transport Director
Transport Department
International Air Transport Association
Montreal, Quebec

Mr. William A. Jordan
Professor of Economics
Faculty of Administrative Studies
York University
Toronto, Ontario

Mr. J.R. Baldwin
Associate Professor of Economics
Department of Economics
Queen's University
Kingston, Ontario

Province of Ontario

Mr. W.D. Burnick, O.C.
Senior External Counsel
Office of Legal Services
Ministry of Transportation and Communications

Mr. David Gurnea
Air Office

Thursday, February 25, 1981

Dr. Richard Schmitz
Associate Professor

Department of Political Science and
Centre for the Study of Registered Industries
McGill University
Montreal, Quebec

Mr. J.M. Fagan
President

Flight Airlines
New London, Connecticut

Institute for Transportation Studies
University of Calgary

Mr. Everett Johnson
Chairman

Mr. J.R. Brent Kishin
Director
Division of Travel and Tourism

Tuesday, March 2, 1981

Council of Union in the Aviation Industry
Canadian Labour Congress

Mr. Donald Montgomery
Chairman of the Council and
Secretary-Treasurer of the Congress

Mr. Murray Randall
National Representative
Canadian Labour Congress

Appendix B

SUBMISSIONS RECEIVED

Air Ontario Limited
Air Transport Association of Canada
City of Brandon, Manitoba
Government of New Brunswick, Minister of Transportation
Government of Newfoundland and Labrador, Department of
Transportation and Communications
Government of Nova Scotia, Minister of Transportation
Government of Prince Edward Island, Department of Highways and Public Works
Government of Yukon, Tourism and Economic Development,
Economic Research and Planning
Northwest Territories, Minister of Government Affairs
The Board of Trade of Metropolitan Toronto
The Canadian Manufacturers' Association
Travel Industry Association of the Northwest Territories
Mr. J. D. Watson, Manotick, Ontario

A copy of the relevant Minutes of Proceedings and Evidence (*Issues Nos. 40, 41, 42, 43, 44, 45, 46, 47, 48, 49, 50, 51, 52, 53, 54 and 55 which includes this report*) is tabled.

Respectfully submitted,

MAURICE A. DIONNE
Chairman

MINUTES OF PROCEEDINGS

TUESDAY, MARCH 23, 1982
(91)

The Standing Committee on Transport met, *In Camera*, at 9:42 o'clock a.m. this day, the Chairman, Mr. Dionne (*Northumberland-Miramichi*) presiding.

Members of the Committee present: Messrs. Benjamin, Bockstael, Corbin, Mrs. Côté, Messrs. Deniger, Dionne (*Northumberland-Miramichi*), Ellis, Flis, Harquail, Mayer, McDermid, Nowlan and Turner.

Other Member present: Mr. Daudlin.

In attendance: From the Parliamentary Centre for Foreign Affairs and Foreign Trade: Mr. Peter Dobell, Director; Mr. Cary Swoveland, Transportation Economist; Mr. Robert Obadia, Air Transportation Consultant; Mr. Timothy Denton, Lawyer and Consultant in regulatory matters and Mr. Gregory Kane, Counsel.

The Committee resumed consideration of its Order of Reference with respect to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981". (*See Minutes of Proceedings, Thursday, January 28, 1982, Issue No. 40*).

The Committee proceeded to consider its draft report to the House with respect to the document, entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981".

On motion of Mr. Bockstael, seconded by Mr. Nowlan, Mr. Deniger was elected Vice-chairman of the Committee.

On motion of Mr. Corbin, seconded by Mr. Turner, it was agreed,—That the Committee print an additional 2000 copies of Issue No. 55 of the Committee's Minutes of Proceedings and Evidence with a special cover.

On motion of Mr. Deniger, seconded by Mr. Nowlan, it was agreed,—That the Committee hire a designer or an advertising agency to prepare camera ready artwork for the design of its cover relating to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981".

At 12:00 noon, the Committee adjourned until 3:30 o'clock p.m. this day.

AFTERNOON SITTING

(92)

The Standing Committee on Transport met, *In Camera*, at 3:38 o'clock p.m. this day, the Chairman, Mr. Dionne (*Northumberland-Miramichi*) presiding.

Members of the Committee present: Messrs. Benjamin, Bockstael, Campbell (*LaSalle*), Deniger, Dionne (*Northumberland-Miramichi*), Ellis, Flis, McDermid and Nowlan.

In attendance: From the Parliamentary Centre for Foreign Affairs and Foreign Trade: Mr. Peter Dobell, Director; Mr. Cary Swoveland, Transportation Economist; Mr. Robert Obadia, Air Transportation Consultant; Mr. Timothy Denton, Lawyer and Consultant in regulatory matters and Mr. Gregory Kane, Counsel.

The Committee resumed consideration of its Order of Reference with respect to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981. (*See Minutes of Proceedings, Thursday, January 28, 1982, Issue No. 40.*)

The Committee resumed consideration of its draft report to the House with respect to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981".

At 5:20 o'clock p.m., the Committee adjourned until 9:30 o'clock a.m., Thursday, March 25, 1982.

Santosh Sirpaul

Clerk of the Committee

THURSDAY, MARCH 25, 1982

(93)

The Standing Committee on Transport met, *In Camera*, at 9:45 o'clock a.m. this day, the Chairman, Mr. Dionne (*Northumberland-Miramichi*) presiding.

Members of the Committee present: Messrs. Benjamin, Bockstael, Campbell (*LaSalle*), Corbin, Deniger, Dionne (*Northumberland-Miramichi*), Ellis, Flis, McDermid, Nowlan and Siddon.

In attendance: From the Parliamentary Centre for Foreign Affairs and Foreign Trade: Mr. Peter Dobell, Director; Mr. Cary Swoveland, Transportation Economist; Mr. Robert

Obadia, Air Transportation Consultant; Mr. Timothy Denton, Lawyer and Consultant in regulatory matters and Mr. Gregory Kane, Counsel.

The Committee resumed consideration of its Order of Reference with respect to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981". (See *Minutes of Proceedings, Thursday, January 28, 1982, Issue No. 40*).

The Committee resumed consideration of its draft report to the House with respect to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981".

At 12:00 noon, the Committee adjourned until 9:30 o'clock a.m., Tuesday, March 30, 1982.

Santosh Sirpaul
Clerk of the Committee

TUESDAY, MARCH 30, 1982
(94)

The Standing Committee on Transport met, *In Camera*, at 9:42 o'clock a.m. this day, the Chairman, Mr. Dionne (*Northumberland-Miramichi*) presiding.

Members of the Committee present: Messrs. Benjamin, Bockstael, Corbin, Mrs. Côté, Messrs. Dionne (*Northumberland-Miramichi*), Ellis, Flis, Forrestall, Gour, Harquail, MacBain, Mayer, McDermid, Nowlan, Reid (*St. Catharines*), Scott (*Hamilton-Wentworth*) and Turner.

In attendance: From the Parliamentary Centre for Foreign Affairs and Foreign Trade: Mr. Peter Dobell, Director; Mr. Robert Obadia, Air Transportation Consultant and Mr. Timothy Denton, Lawyer and Consultant in regulatory matters.

The Committee resumed consideration of its Order of Reference with respect to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981". (See *Minutes of Proceedings, Thursday, January 28, 1982, Issue No. 40*).

The Committee resumed consideration of its draft report to the House with respect to the document entitled, "Proposed Domestic Air Carrier Policy (Unit Toll Services), August 1981".

The report, as amended, was carried on division.

On motion of Mr. Nowlan, seconded by Mr. Gourd, it was agreed,—That the Chairman be authorized to make such typographical and editorial changes which may be necessary without changing the substance of the draft report to the House.

Ordered,—That the Chairman report to the House.

On motion of Mr. Bockstael, seconded by Mr. McDermid, it was agreed,—That the Committee authorize the printing of Issue no. 55, which contains its Ninth Report to the House, in a tumble format.

It was agreed,—That immediately after the tabling of the report to the House, a press conference be called to highlight the major elements of the report.

It was agreed,—That a meeting of the sub-committee on Agenda and Procedure be called at 9:30 o'clock a.m., Thursday, April 1, 1982.

At 11:06 o'clock a.m. the Committee adjourned to the call of the Chair.

Santosh Sirpaul
Clerk of the Committee