
Edmonton City Centre Airport Audit

November 19, 2003

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Edmonton City Centre Airport Audit

I. Introduction

This audit of the Edmonton City Centre Airport by the City of Edmonton's Office of the City Auditor (OCA) was conducted in response to direction from City Council in April 2003. The City Centre Airport is owned by the City and is leased to the Edmonton Regional Airports Authority ('Edmonton Airports').

Edmonton Airports is a board-governed, not-for-profit organization whose mission is to "manage its airports in a safe, secure, and commercially focussed manner with emphasis on customer satisfaction. Through optimal air service, facilities and resources, [Edmonton Airports is] a significant contributor to, and a catalyst for, regional/provincial economic growth." ¹ The City Centre Airport is one of four airports (City Centre, International, Villeneuve and Cooking Lake) operated by Edmonton Airports.

Concurrent with the OCA review, Edmonton Airports conducted a strategic study to review the City Centre Airport's role within the system of airports it manages and to define a 10-year business plan for the City Centre Airport. The results of this strategic study are to be made public in November 2003. Consequently, the contents of this particular 10-year business plan (including financial and capital forecasts) were not considered within the scope of the OCA's audit.

II. Background

Prior to 1960, the City Centre Airport served as the exclusive commercial airport in the Edmonton region. In 1960, national and international air traffic was transferred to the newly constructed Edmonton International Airport, south of Edmonton.

As a result, the City Centre Airport (known then as the Edmonton Industrial Airport and later as the Edmonton Municipal Airport) became a regional airport, offering scheduled air services to major centres in Alberta, neighboring provinces and the Yukon and Northwest Territories. It was also an important centre for general aviation.

Today, the City Centre Airport functions primarily as a general aviation airport, but also maintains some limited scheduled air service to various Alberta communities. The events leading to its current role are outlined below.

Ongoing Uncertainty

Uncertainty concerning the future of the City Centre Airport began in the 1950s when the International Airport was proposed. The City subsequently sold portions of the City

¹ *Edmonton Airports 2002 Annual Report*

Centre Airport surplus lands and limited the City Centre Airport's role to serving regional air traffic.

Later, a 1987 study² commissioned by the City acknowledged that the airport was struggling with its role, with general airport users perceiving a lack of confidence in airport stability, poor investor confidence, poor tenant and customer relations due to lack of communication, and a lack of clear identity.

In 1992, a petition was presented to City Council, forcing a referendum to resolve whether or not City Council should continue to own, operate and manage the City Centre Airport and maintain its scheduled air service. The citizens of Edmonton voted by a slim margin to keep the airport functioning as a scheduled service airport. Three years later, the outcome of the 1992 referendum was revisited through another referendum.

During the 1995 referendum debate, Edmonton Airports produced a five-year strategic plan, *Airports 2000*, detailing its vision for air service in the Edmonton region.³

Edmonton Airports' Strategic Plan

According to Edmonton Airports, a significant weakness of the City Centre Airport in 1995 was the uncertainty that resulted from the lack of a clear direction for the airport.⁴ To remedy this, Edmonton Airports proposed the amalgamation of all airport facilities in the region under Edmonton Airports' management, where each airport would serve a complementary, rather than a competing, role:

- *International Airport* – regional and long-haul domestic and international passenger and cargo flights, long-haul charter flights;
- *City Centre Airport* – corporate and general aviation, charter flights, medevac flights, military, light cargo operations and the further development of the aerospace industry;
- *Cooking Lake Airport* – recreational flying, general aviation, float plane base, and support services; and
- *Villeneuve Airport* – recreational flying, general aviation, flight training, and support services.

Under its management, Edmonton Airports foresaw improving the City Centre Airport's financial position and funding all capital improvements through the cash flow generated from the system of airports. The strategic plan was central to the debate on the City Centre Airport's future and the outcome of the 1995 referendum.

² *Edmonton Municipal Airport Marketing Communication Plan* (1987), prepared for the City of Edmonton by The Focal Group Limited.

³ *Edmonton Airports Strategic Plan: Airports 2000* (1995).

⁴ *Edmonton Airports Strategic Plan: Airports 2000* (1995) Appendix B, p. 8.

1995 Referendum

The results of the October 16, 1995, referendum indicated that over three-quarters of voters believed that the City should promote moving scheduled air passenger service to the Edmonton International Airport.

The 1995 referendum redefined the role of the City Centre Airport from being a scheduled passenger and general aviation airport with heavy traffic to being predominantly a general aviation airport catering to charters, corporate planes, private operators, and emergency service.

Based on the results of this referendum, the City of Edmonton entered into a lease with Edmonton Airports on March 25, 1996, to have it manage the City Centre Airport facilities for a term of fifty-six years.

The Lease

Under the lease, Edmonton Airports assumes the full and sole responsibility for the operation and management of the City Centre Airport. The lease requires that ongoing repairs and maintenance be to a standard that will substantially preserve the condition and state of the City Centre Airport that existed on the date of the lease. At the end of the term on March 31, 2052 (unless otherwise extended), Edmonton Airports is obligated to return the City Centre Airport to the City.

The lease directs that Edmonton Airports maintain the City Centre Airport as a visual flight rules and instrument flight rules precision-approach public airport, providing 7x24 landing capability, and offer general aviation services (e.g., private planes, small charters and air ambulances). The lease acknowledges that Edmonton Airports intended to restrict scheduled air service and permit other uses not incompatible with the operation of an airport.

As long as Edmonton Airports respects the terms and conditions of the lease, it shall “peaceably and quietly hold and enjoy the [City Centre Airport] for the Term without hindrance or interruption by the City.”⁵ However, if there is an event of default by Edmonton Airports, the City has the right to terminate the lease if Edmonton Airports does not remedy the default within a prescribed timeframe. Events of default include defaults in payment of rent or any additional rent, defaults in the performance of any of the covenants, agreements, provisions, stipulations or conditions of the lease, and if Edmonton Airports abandons the City Centre Airport. The City and Edmonton Airports could also mutually agree to an earlier termination of the lease.

If the lease were terminated prematurely, scheduled air service at the City Centre Airport would likely remain restricted, at least for a period of time, due to an agreement the City made with Edmonton Airports in 1999. To enable Edmonton Airports to obtain funding for the International Airports air terminal redevelopment (ATR) project, the City of Edmonton committed to maintaining whatever passenger access restrictions were in

⁵ “Quiet Enjoyment” clause (Article 34.32 of the lease)

place, if the lease were terminated prematurely and the ATR financing had yet to be repaid.⁶

This agreement was designed to mitigate the risk of unrestricted scheduled passenger service at the City Centre Airport diverting passenger traffic and revenues from the International Airport, thereby decreasing Edmonton Airports' ability to repay the air terminal financing. In return for providing the "comfort" letter, the City sought and received assurances from Edmonton Airports that all revenue derived from the City Centre Airport, including land development revenue, would be applied to operate and maintain the City Centre Airport.

III. Audit Objectives

The objectives of this audit were as follows:

1. To assess Edmonton Airports' and the City of Edmonton's overall compliance with the terms of the lease agreement.
2. To assess the reasonableness of Edmonton Airports' proposed 10-year capital program (buildings, paved surfaces, utility systems, maintenance equipment, and vehicles) for improvements at the City Centre Airport.
3. To provide assurance regarding the financial position and projections of the City Centre Airport and the overall financial position of Edmonton Airports.
4. To assess Edmonton Airports' efforts to date in fostering business development and stability at the City Centre Airport.
5. To assess the impact of the January 2004 access policy changes and of further restrictions in scheduled service on the City Centre Airport's economic role.

IV. Scope and Methodology

As was noted earlier, the OCA did not include in its audit a review of Edmonton Airports' November 2003 strategic study that was undertaken concurrently with this audit.

The following elements were included in the OCA audit, in accordance with the audit objectives.

Lease Compliance

The lease forms the basis of the relationship between the City of Edmonton and Edmonton Airports concerning the management and maintenance of the City Centre Airport. It establishes the City's expectations of Edmonton Airports and provides several indemnity clauses that protect the City from liabilities that are incurred during the term of the lease. Throughout the review, the OCA assessed Edmonton Airports' and the City of Edmonton's adherence to key clauses within the lease.

⁶ The bonds used to finance the air terminal redevelopment project mature in November 2030.

Capital Program

This portion of the review focused on historical and future capital programs at the City Centre Airport. Audit work focused on evaluating the justifications, proposed schedules, and estimated costs associated with the planned capital program. A sample of the capital projects for buildings, paved surfaces, and utility systems was selected for more detailed review. The review for fleet and equipment considered all related capital projects.

Financial Review

This portion of the review included a high level review of Edmonton Airports' historical financial information and a more detailed financial assessment of the City Centre Airport, including forecasts. The OCA reviewed relevant documents (e.g., financial reports from other airports, consultant reports, strategic plans, management letters resulting from the most recent financial audits, etc.) and met with financial representatives of Edmonton Airports and their maintenance and operations contractor's staff at the City Centre Airport during this evaluation.

Business Development

This portion of the review assessed Edmonton Airports' investment in aviation through business development, marketing and communications initiatives. To assess the adequacy of Edmonton Airports' efforts, the OCA reviewed the execution of the 1995 City Centre Airport business plan and the subsequent annual business plans and annual reviews required to be submitted to the City under article 28 of the lease. The OCA supplemented these data sources with interviews, surveys, and various reports.

Survey of City Centre Airport Businesses and other Establishments

The OCA, with the assistance of Nichols Applied Management, administered a survey to 85 operating businesses, tenants, and other establishments with a presence at the City Centre Airport. The purpose of the survey was to obtain baseline economic data, to gather future plans and prospects at the City Centre Airport, and to survey attitudes regarding airport management activities. Edmonton Airports reviewed and provided feedback on the survey prior to the survey's administration.

This confidential survey was administered in June and July of 2003. The response rate was 94% (80 of 85 establishments), resulting in an accuracy of within ± 2.7 percentage points, 19 times out of 20. The timing of the survey may have impacted the intensity of the tenants' responses. Tenants were surveyed approximately six months after Edmonton Airports suspended major marketing initiatives and subsequently commissioned a strategic study concerning City Centre Airport's role in the 4-airport system. The survey also followed an announcement by Edmonton Airports of a change in the City Centre Airport's Access Policy.

Follow-up interviews were conducted in August 2003 with a number of businesses likely to be affected by the operational changes occurring at the City Centre Airport effective January 1, 2004. These interviews were designed to probe the expected impacts (direct

and indirect) of the planned curtailment of air cargo operations and scheduled passenger operations using 19-seat aircraft at the City Centre Airport.

Economic Overview and Impact Analysis

The OCA's review necessarily included some examination of the City Centre Airport's recent development patterns and current economic role, contributions, and issues. This work provided a context and baseline from which to assess the impacts of planned and potential changes to the City Centre Airport's Access Policy, with a particular focus on impacts to the airport and to the airport business community.

It was beyond the scope of the OCA's review to assess the full costs and benefits of the policy changes to the regional airport system or the city's economy as a whole, or to attempt to quantify the net effects that might accrue from parallel initiatives taken by Edmonton Airports to mitigate any adverse impacts at the City Centre Airport. Accordingly, the analyses provided do not purport to advise as to the overall impacts and merits of the policy changes considered.

Parallel to the OCA audit, Edmonton Airports engaged two consulting firms to measure and evaluate the success of Edmonton Airports in achieving the stated benefits of consolidation forecasted in 1995, and to summarize the results in a "consolidation report card."⁷ Prior to this initiative, Edmonton Airports had commissioned an economic impact study to assess the Edmonton-based employment impact of ongoing operations at the International Airport in 2002.⁸

V. Economic Role of the City Centre Airport

Designated primarily as a general aviation facility, the City Centre Airport accommodates a diverse clientele of corporate, government, and private aircraft operators, as well as pilot training and medevac services. A key attribute of the airport for individual passengers and for corporate, government, and other users is its central location within the City and surrounding region and its associated convenience and accessibility to the city's downtown.

A number of aviation-related support businesses – for example, fuelling facilities, aircraft repair, maintenance, and inspection services, and aerial surveying operations – are situated on or adjacent to the airport property and serve both on-site and regional customers. The airport also provides scheduled air services connecting to various centres in Alberta including Calgary, Lethbridge, Fort McMurray, Grande Prairie, High Level, and Peace River through smaller regional aircraft. In recent years, non-aviation establishments have also located at the Airport (e.g., the Amiskwaciy Academy, the Workers' Compensation Board (WCB), Via Rail, and the North Edmonton Armories).

⁷ *2003 Review of Air Service Consolidation at Edmonton International Airport*, prepared by InterVISTAS Consulting Inc. and Sypher Mueller International for Edmonton Airports.

⁸ *Edmonton International Airport Economic Impact Study* (March 2002) prepared by InterVISTAS Consulting, Inc. for Edmonton Airports.

An interconnected nucleus of about 85 commercial and non-commercial establishments operates on or immediately adjacent to the airport property. Approximately 90% of the establishments operating at or immediately adjacent to the Airport are associated directly or indirectly with aviation activities, and they account for three-quarters of the airport employment base. About 85% of the Airport's revenues derive from aircraft and passenger fees and aviation-related tenants.

Eighty of those operations responded to a survey carried out on behalf of the OCA during the audit review period. They employ approximately 1,160 full-time and 225 part-time staff having a total payroll of more than \$65 million annually. Of the total full-time employees, over 800 are employed in aviation or aviation-related businesses. Most seasonal and part-time jobs at the airport are also aviation-related. The commercial businesses (excluding the scheduled carriers) at the airport generate revenues in excess of \$100 million annually but the importance of non-aviation tenants such as the WCB has increased markedly over the past two-to-three years.

Reported levels of aviation activity at the airport have increased in recent years. That trend is evident also from the survey of airport businesses conducted by the OCA: two-fifths of airport businesses reported relatively stable revenues in recent years, but a higher proportion of businesses – especially the larger firms – have experienced growth versus decline in their business volumes. An examination of responses for aviation-related firms at the airport indicate that employment levels over the past three years at the airport have increased by about 17%. The inclusion of new non-aviation establishments such as the WCB and the Amiskwacy Academy would add to the growth of aggregate employment.

VI. Aviation Activity at the City Centre Airport

From 1997 to 2002, general aviation aircraft movements increased by roughly 12% and scheduled airline aircraft movements have more than doubled. As a result, total aircraft movements have increased by 23% since 1997 at the City Centre Airport (see Table 1).

Table 1: City Centre Airport Aircraft Movements, 1997-2002⁹

Year	General Aviation	Scheduled Airlines	Total
1997	69,666	9,150	78,816
1998	72,468	12,018	84,486
1999	77,273	14,122	91,395
2000	81,561	12,950	94,511
2001	75,355	21,683	97,038
2002	77,800	19,407	97,207

Note: 1997 was the first full year of operation under Edmonton Airports' management.

⁹ *Aircraft Movement Statistics 2001 & 2002 Annual Reports (TP577)*, prepared by Transport Canada.

General aviation aircraft movements can be broken down further into itinerant and local aircraft movements, as is illustrated in Table 2. Itinerant aircraft movements are aircraft landings or takeoffs that are reported on the basis of “place arrived from” or “place departed to” (e.g., chartered, government, and private flights). In contrast, local aircraft movements are flights that do not leave the aircraft control circuit (e.g., flight training). Since 1997, itinerant general aviation aircraft movements have increased by 5% and local general aviation aircraft movements have increased by 56%.

Table 2: City Centre Airport General Aviation Aircraft Movements, 1997- 2002

Year	Itinerant	Local	Total
1997	60,560	9,106	69,666
1998	62,271	10,197	72,468
1999	66,039	11,234	77,273
2000	70,766	10,795	81,561
2001	65,916	9,439	75,355
2002	63,600	14,200	77,800

Scheduled Air Service: The results of the 1995 referendum directed that the City promote moving scheduled air passenger service to the International Airport and it was on this basis that Edmonton Airports assumed management of the City Centre Airport. In article 6.3 of the lease, the City formally acknowledged that Edmonton Airports would be restricting scheduled air passenger service at the City Centre Airport.

The 1995 strategic plan recognized that capital improvements would be necessary at the International Airport to accommodate the additional scheduled air traffic from the City Centre Airport. Once these facility improvements were made, Edmonton Airports envisioned that all scheduled air service would be transferred to the International Airport by 1998. Edmonton Airports also stated that after consolidation of scheduled air services at the International Airport, no new entrant scheduled service carriers would be permitted to operate from the City Centre Airport.¹⁰

After consolidation, Edmonton Airports chose to allow small, 10-seat aircraft to provide scheduled service at the City Centre Airport, creating a niche market that did not exist prior to consolidation. In 1999, in response to requests from carriers at Edmonton City Centre Airport, Edmonton Airports revised the access policy to allow carriers to utilize aircraft with up to 19 seats, provided the carriers respected the 10-passenger cap. This allowed the users greater flexibility in their choice of aircraft and accommodated broader business uses.

According to Edmonton Airports, the International Airport will soon be able to accommodate scheduled air carriers at its north terminal, reinforcing the International Airport’s role as a hub airport. As a result, effective January 1, 2004, aircraft with more than 10 seats may no longer provide scheduled air service out of the City Centre

¹⁰ *Edmonton Airports Strategic Plan: Airports 2000* (1995), p. 9.

Airport. According to Edmonton Airports, the difficulty in, and expense of, monitoring the 19-seat aircraft and enforcing the access policy's 10-passenger cap provided additional impetus for the access policy change.

The City Centre Airport currently accounts for roughly 3% of all enplaned and deplaned scheduled air passengers that utilize the regional airports system. A recent survey of passengers at the City Centre Airport conducted by WesTrends Research indicated that Edmonton's downtown was the destination for 63% of arriving passengers.¹¹ The same survey showed that 96% of respondents cited "convenience", 64% "less security hassles", and 44% "cost" as factors for using the airport. Persons travelling for business or combined business/pleasure purposes account for more than 95% of passengers using the airport, according to the WesTrends survey, and those travellers are shown to be frequent users of the City Centre Airport.

A recent intercept survey conducted on behalf of Edmonton Airports corroborated the convenience factors seen by City Centre Airport passengers, who especially noted the airport's location and flight-scheduling advantages and perceived benefits in terms of flight times.¹² Those benefits are particularly valued by business and commercial users flying "point-to-point" to or from Edmonton who do not require onward scheduled air service connections.

The City Centre Airport historically has had strong ties to the North. While many private, corporate, government, charter, and medevac air services continue to connect the airport with northern Alberta communities, City Centre Airport's relative importance in respect of scheduled air services diminished when the majority of scheduled service was consolidated at the International Airport. Annually, the City Centre Airport now accounts for approximately 5% of the 700,000 available scheduled passenger seats to northern Canada. Given the City Centre Airport does not provide scheduled air passenger services to northern communities outside of Alberta, a better reflection is the percentage of passenger seats to northern Alberta. The City Centre Airport currently provides 10% of the available 340,000 passenger seats to northern Alberta.

The City Centre Airport's importance to the North is more significant if the frame of reference is confined to particular northern communities, as is demonstrated in Table 3. The analysis of the proportionate number of seats, flights and carriers provides a measure of the corresponding capacity, convenience and competition. From Edmonton to Peace River and High Level, the City Centre Airport accounts for a significant number (47% and 70%, respectively) of their passenger seats and the majority (64% and 81%, respectively) of their scheduled flights. For the communities of Fort McMurray and Grande Prairie, the number of available passenger seats from the City Centre Airport is small compared to the International's (5% and 7%, respectively), but the City Centre Airport accounts for almost one-third of the scheduled flights available to these communities. In High Level, carriers from the City Centre Airport are providing both the majority of the service and the majority of the competition.

¹¹ *City Centre Airport Passenger Survey* (April 2003) prepared by WesTrends Research.

¹² *Passenger Intercept Survey* (September 2003) prepared by Deloitte & Touche/Sypher.

Table 3: The City Centre Airport's Proportionate Traffic to Select Northern Cities*

City	Passenger Seats	Flights	No. of Carriers
Fort McMurray	5%	30%	1/3
High Level	70%	81%	2/3
Grande Prairie	7%	27%	1/3
Peace River	47%	64%	1/2

* Compared to the International Airport and City Centre Airport, combined.

Cargo: In 2002, dedicated cargo activity at the City Centre Airport represented just over 1% of the activity in the 4-airport system.¹³ As of January 1, 2004, Edmonton Airports will prohibit aircraft whose primary purpose is transporting cargo for direct or indirect commercial gain from using the City Centre Airport. Edmonton Airports directed this change in order to create critical mass at the International Airport cargo terminal and provide clarity for the roles of each of its airports. This is within Edmonton Airports' authority under the lease.

The three cargo operations that have operated at the City Centre Airport have since relocated or are in the process of relocating to the International Airport. All three provided cargo service to Calgary only. The shipping of cargo incidental to any tenant/user's primary business will be permitted under the January 2004 access policy.

VII. Observations and Analysis

A. Lease Compliance

In general, Edmonton Airports has been in compliance with the lease. There were three instances when Edmonton Airports was not in compliance and had not been notified by the City. The City's Law Branch has advised that none of these instances of non-compliance is considered a fundamental breach of the lease. The instances of non-compliance concerned chattels, insurance, and reporting.

Chattels: Article 13 of the lease states that Edmonton Airports must pay the City for any chattels in the lease that are transferred from the City Centre Airport or sold from its inventory. In turn, the City must deposit the funds in the City Centre Airport Reserve Fund.

In 1996, Edmonton Airports transferred two passenger loading bridges and furniture, for a total book value of \$680,262, to the International Airport. Edmonton Airports did not notify the City of Edmonton in writing of the removal of the chattels from the City Centre Airport as required in the lease and no funds were exchanged. Instead, Edmonton

¹³ *Historical Analysis of Edmonton's Northern Air Services*, prepared for Edmonton Airports by InterVISTAS Consulting, December 17, 2002.

Airports funded capital improvements at the City Centre Airport from Edmonton Airports' general revenues.

The City's Law Branch confirmed that this does not constitute a fundamental breach of the lease, and there are no losses or damages that should be pursued by the City as a result.

Insurance: Subsection 20.1.4 of the lease requires that, as of 1998 and at intervals of no more than five years, Edmonton Airports obtain a property appraisal for the City Centre Airport to ensure that it is appropriately insured.

Edmonton Airports has not obtained a property appraisal, choosing instead to "over-insure" the City Centre Airport. The City's Law Branch has confirmed that this is not a fundamental breach of the lease, and has advised that Risk Management should consider whether or not it would be prepared to waive the requirement for a property appraisal in accordance with the lease and accept Edmonton Airport's alternative approach.

Reporting: Article 28.2 of the lease requires that Edmonton Airports provides to the City "an annual business plan, including a capital expenditure plan, for the upcoming year and for a forecast five-year period, with respect to the operation of the [City Centre Airport]." Associated with this requirement is Article 28.3 of the lease that requires that Edmonton Airports provides to the City "an annual review of the operation of the airport...which shall include...a report on performance relating to the business plan and objectives established by [Edmonton Airports] for the previous year and, as applicable, the past five-year period."

Edmonton Airports has routinely provided 5-year schedules of capital projects to the City as part of its annual business plan submission. In contrast, the City Centre Airport business plans have not included 5-year forecasts, focussing instead on the upcoming year. As a result, the annual reviews have also been limited to a review of the past year's performance. Edmonton Airports did not receive feedback on its submissions from the City and was unaware of its non-compliance.

City's Responsibility

Given the lease agreement is the primary means by which the City can assess Edmonton Airports' management of the City Centre Airport, it is important that the City regularly monitor and report on compliance to all key clauses of the lease. This is occurring in the majority of instances. Most notably, considerable effort is exerted by both Edmonton Airports and the City in complying with article 25 of the lease, which outlines the process and criteria for determining whether or not sub-leases may be assigned to prospective tenants.

The City needs to ensure that the appropriate City personnel are formally provided with the responsibility and authority, as well as the corresponding accountability, to monitor all key clauses of the lease.

B. Capital Program

A fundamental requirement for analysis of the City Centre Airport budgeted capital program is the obligation of Edmonton Airports to maintain the infrastructure at levels of repair consistent with the lease agreement. Article 16.2 of the lease states that Edmonton Airports has the following obligation:

The Tenant at its sole cost and expense shall during the Term continuously, actively and diligently keep, operate and maintain in good order and condition the [City Centre Airport] and shall at all times make any and all necessary repairs, maintenance, replacements, alterations, additions, changes, substitutions and improvements, ordinary or extraordinary, foreseen or unforeseen, structural or otherwise, and keep the [City Centre Airport] in good and substantial repair, reasonable wear and tear and damage by fire, lightning, tempest or other casualties only excepted. Such repairs and maintenance shall be in all respects to a standard at least substantially equal in quality of material and workmanship to the condition and state of the [City Centre Airport] on the Commencement Date. The Tenant's obligation hereunder to repair and maintain shall also be deemed to include all utilities in, on, under or over the [City Centre Airport], other than those utilities which are protected by easements or utility rights of way registered against Schedule "A" lands, and are to be maintained by the City or third parties pursuant to the terms thereof. For the purposes of this Section, the term "repair" shall include without limitation, replacement or renewals and the term "maintain" shall include without limitation, servicing, cleaning, painting and decorating. Notwithstanding the aforesaid, the Parties hereto agree that the Tenant's obligation hereunder to repair and maintain shall not include the Hangars.

As stated in article 17.4 of the lease, Edmonton Airports cannot demolish or remove from the City Centre Airport any existing or new facility (i.e., buildings, structures, improvements and fixtures) or part thereof without first obtaining the written consent of the City. Changes to the facilities would directly impact the level of capital investment required to maintain them.

Article 16.6 of the lease grants the City the right to enter the City Centre Airport premises to determine its condition or state of repair and maintenance and/or to verify that Edmonton Airports is complying with the provisions of the Lease. In the event these inspections determine maintenance deficiencies, the City has the right to direct Edmonton Airports to remedy such deficiencies.

The City's Lands and Buildings Branch leasing staff conducts, on an ad-hoc basis, "walk through inspections". To-date, no maintenance deficiencies have been noted by the City. The City could conduct (at some future date) detailed facility inspections involving trade staff and professionals to ascertain the condition of the complete infrastructure inventory.

City Centre Airport Safety Status

In its 1995 strategic plan, Edmonton Airports indicated that it planned average capital investments of about \$1.5 million per year from 1997 to 2000, totalling approximately \$6 million. Of these capital investments, major overlays of the two runways were planned at a total cost of \$3 million. The actual investment in paved surfaces during that time, however, was \$1.6 million, with a portion of the planned improvements being deferred.

These deferrals did not impact the City Centre Airport's Certified Airport status with Transport Canada. In its July 1998 Safety Inspection Audit, Transport Canada concluded that the City Centre Airport met the applicable regulations and standards as required to continue airport operations. The OCA confirmed the continued safety of the airport through correspondence with a Transport Canada official who stated:

“...as of [October 2, 2003] we at Aerodrome Safety Edmonton have no immediate Safety Concerns at Edmonton City Centre Airport. This airport is Certified and meets all our regulatory requirements to be a Certified Airport. We will be conducting an Audit of this Airport in April/May 2004...”

In addition, 71% of the respondents to the tenant survey rated Edmonton Airports' maintenance of City Centre Airport aviation facilities (such as runways and taxiways) as good or very good.

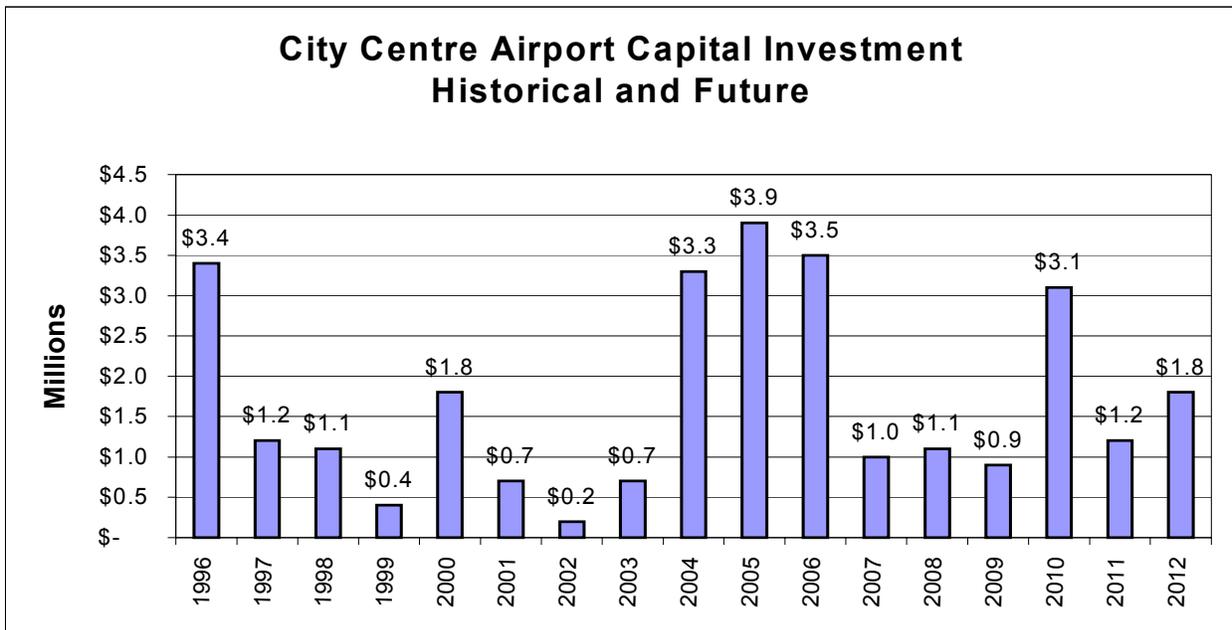
Historical Capital Investment

From 1996 to 2002, the total investment in capital improvements at the City Centre Airport has totalled \$8.4 million. Of this, \$3.8 million was from the Airport Reserve Fund,¹⁴ \$1.0 million was from the Federal government's Airport Capital Assistance Program (ACAP), and the remaining \$3.6 million was subsidized from Edmonton Airports' general revenue. The capital improvements addressed both airside and tenant servicing needs.

Over this period of time, the annual capital investment at the City Centre Airport has generally declined from a high of \$3.4 million, funded through the Airport Reserve Fund, to a low of \$0.2 million (see Figure 1). Nonetheless, the patterns of capital expenditures reflect the normal capital planning process at the City Centre Airport, where investments are made on a timetable that is consistent with the lifecycle replacement timetable for the various classes of assets. The exception is 2002, where, while the future operation of the City Centre Airport was being reviewed, capital investments that could be postponed without significant operational impacts were deferred to subsequent years.

¹⁴ Consistent with the lease agreement, the City provided Edmonton Airports with the proceeds from the Airport Reserve Fund, totalling \$3.8 million, to help fund future capital expenditures at the City Centre Airport.

Figure 1



Future Capital Investments

Edmonton Airports currently has a program in place that provides forecasts for capital needs for all infrastructure categories (buildings, paved surfaces, utility systems, and fleet and equipment) at the City Centre Airport through 2020. The program is deemed necessary to maintain, rehabilitate or replace the infrastructure to the level required in the lease and is consistent with the airport’s current operational requirements.

During preparation of the Terms of Reference for this audit, the OCA obtained a 10-year capital plan for 2003 to 2012, dated January 2003. When audit fieldwork started in April 2003, Edmonton Airports' Board of Directors directed that its administration perform an internal review and update of this program to further refine the planned scope of work and improve the accuracy of the cost estimates. The update was extended to include an additional eight years (2013 - 2020).

In June 2003, Edmonton Airports provided the updated capital analysis to the OCA. The OCA review focused on this revised capital program, but only for the period 2003 to 2012 (a period consistent with that stated in the audit's Terms of Reference). Edmonton Airports subsequently performed a more detailed analysis of the fleet and equipment 10-year capital program and provided this further update to the OCA in October 2003. The historical expenditures and the various estimates are provided in Table 4, below.

Table 4: City Centre Airport Capital Program Overview

Infrastructure Category	Historical Expenditures	January 2003 Estimates	Revised 2003 Estimates (June to October 2003)	
	1996 – 2002	2003 – 2012	2003 – 2012	2013 – 2020
Buildings	\$2,128,000	\$1,136,700	\$2,390,000	\$875,000
Paved Surfaces	\$1,802,200	\$7,342,000	\$6,451,000	\$6,137,000
Utility Systems	2,762,100	\$6,681,000	\$6,963,000	\$1,048,000
Fleet & Equipment	1,713,700	\$5,425,000	\$4,703,000	\$3,638,000
TOTAL	\$8,406,000	\$20,584,700	\$20,507,000	\$11,698,000
<i>Average Per Year</i>	<i>\$1.2 million</i>	<i>\$2.1 million</i>	<i>\$2.1 million</i>	<i>\$1.5 million</i>

Differences between the January 2003 and revised 2003 estimates are the result of refinements to either the scope of work or refined cost estimates. As part of Edmonton Airports' standard capital project implementation process, it initiates more detailed design and cost estimates the year prior to the actual construction of the specific project. As Edmonton Airports embarked on its strategic study of its system of airports, it postponed some detailed capital estimates pending the outcome of the study.

For each of the identified infrastructure categories, the OCA reviewed documentation to ensure that appropriate engineering studies were carried out to justify the planned scope of work, and that tentative schedules and cost estimates are appropriate for planning purposes. A discussion of each infrastructure category follows:

Buildings: Five building projects have been identified for capital improvement during the period 2003 to 2012. The total capital cost for these projects is estimated at \$2.4 million. The OCA reviewed two projects that account for \$2.2 million (or 91%) of the total planned expenditures. These two projects are for buildings that were originally constructed in the early 1970s.

In May 2003, a team consisting of structural, mechanical, and electrical engineers, as well as architects and a cost consultant updated a 2001 study that merged building

code and upgrade requirements with functional change requests from building occupants. The 2003 evaluation recommended action plans including a prioritized list of projects to address required investments in renovation and upgrades over the next 10 years.

Edmonton Airports' 10-year capital program for buildings is based on engineering studies that justify the planned scope of work, tentative schedule, and cost estimates. The level of information is appropriate for planning purposes.

Paved Surfaces: Thirty-one pavement improvement projects are identified in the capital program for 2003 to 2012. Capital costs for these projects are estimated at \$6.5 million. As noted earlier, Edmonton Airports deferred a portion of its 1997-2000 planned pavement improvements, and these now have to be addressed between 2004 to 2006. The OCA reviewed 10 projects that account for \$4.7 million (73%) of the planned expenditures. Many pavement sections scheduled for improvement were originally constructed in the early 1940s.

In March 2000, an international pavement consulting company joined with a team of local experts to conduct a comprehensive review of pavement conditions at the City Centre Airport. The scope of work included a detailed review of historical records, pavement condition surveys, nondestructive deflection testing, destructive coring and subsurface boring activities, roughness testing, and traffic analysis. This information was used to develop performance prediction models and a 5-year capital improvement plan (2000 to 2004), along with guidelines and recommendations regarding the design and maintenance of pavement surfaces.

In Spring 2003, one of the local experts involved with the original 2000 study reviewed the historical pavement information and developed an updated capital improvement plan based on current inspection data. This update defined the required work, prioritized the required investment over the next 10 years based on a standard Pavement Condition Index, and provided cost estimates. This program is reasonably justified and the information is appropriate for planning purposes.

Utility Systems: Six utility system projects have been identified for capital improvement during 2003 to 2012. The total capital cost for these projects is estimated at \$7.0 million. The OCA reviewed one large project (the storm sewer system that services runways, taxiways and aprons) that accounts for \$6.1 million (or 87%) of the total planned expenditures. The storm sewer system was originally constructed in the early 1940s.

In July 2001, a local engineering company conducted a utility life cycle assessment of the City Centre Airport. The assessment was based on a cursory visual assessment of the existing conditions, work completed by the City of Edmonton in 1992 and industry standard life cycles. The consultant also compiled a database of the existing utility systems for continued use by the City Centre Airport in managing this infrastructure. A high-level estimate was prepared, with the significant qualifier that the majority of the

storm sewer system would need to be inspected by closed circuit television to further refine the estimate.

Edmonton Airports is obligated by the terms of the lease to maintain all utilities that do not fall within easements or utility rights of way. To determine with absolute certainty the correlation between the location of utility infrastructure and the location of the relevant easement or rights of way, the assistance of further parties, including a land surveyor and utilities locator, would be required. However, preliminary paper analysis conducted jointly by the OCA, and the City's Law Branch, Drainage Services, and Leasing & Property Section does indicate that some of the minor drainage improvements identified by the City Centre Airport appear to be a City responsibility. To clearly identify the extent of its obligations to maintain utility infrastructure, Edmonton Airports needs to work with the City and other third parties to ascertain more completely responsibility for underground related improvements.

The utility system capital program is based on high-level estimates, with due consideration to component life cycle requirements. It is reasonably justified and the information is appropriate for strategic planning purposes.

Fleet and Equipment: In May 2003, a consultant documented the results of a site survey and fleet audit of Edmonton Airports' proposed 10-year fleet and equipment program for the City Centre Airport. During the course of the OCA's audit, the OCA raised concerns regarding the adequacy of the analysis supporting the proposed program.

Edmonton Airports then undertook a more formal analysis by engaging the services of an engineering company with the appropriate expertise to evaluate airport fleet and equipment requirements and the procedures used by Edmonton Airports to complete the capital program. This more recent analysis of the entire vehicle and equipment fleet was made available to the OCA on October 1, 2003.

Based on a comparison of similar operations, potential equipment efficiencies and the airfield configuration at the City Centre Airport, the engineering company recommended changes to the original fleet and equipment capital replacement program. Based on the recommendations, a \$4.7 million investment in fleet and equipment is now planned for 30 units over the next ten years. Consistent with the City Centre Airport's internal equipment replacement methodology, Edmonton Airport has completed more precise analyses for the units scheduled for replacement or major repair in 2003.

The October 2003 fleet and equipment capital program is reasonably justified and the information provided is appropriate for current year budget needs and planning purposes.

Funding Capital Improvements

At the time of consolidation, one of Edmonton Airports' core principles was that capital requirements would be funded on a system basis. In other words, the airports as a system would generate sufficient cash flows to fund all capital requirements.

The City Centre Airport continues to have insufficient revenues to fund all of its capital improvements needs. In the past, Edmonton Airports has funded City Centre Airport capital improvements through the Airport Reserve Fund received from the City, the federal Airport Capital Assistance Program and from Edmonton Airports' general revenues.

Given the magnitude of capital improvements required, the Airport Reserve Fund was depleted within the first few years after consolidation. And, although Airport Capital Assistance Program funding was successfully obtained in two instances, Edmonton Airports cannot rely on this source for ongoing funding. Edmonton Airports does, however, continue to make applications as the opportunities arise.

While Edmonton Airports has subsidized capital improvements in the past, it has indicated that its tenants and airlines at the International Airport do not support the subsidization of the City Centre Airport. These stakeholders assert that the subsidization unfairly increases the costs at all airports and, as a result, the City Centre Airport should be expected to fund its own capital improvement needs. Edmonton Airports has now adopted this approach, with the expectation that the City Centre Airport will fund both its future and historical capital improvements, in addition to its operating costs, from its own revenues and other funding sources.

Appendix 1 outlines in more detail the progression of changes in Edmonton Airports' funding philosophy toward the City Centre Airport.

C. Financial Review

The OCA conducted an analysis of the City Centre Airport's financial position, including its revenues, expenses, net earnings, cash flow, and short and long-term debt. In addition, the OCA performed a high-level analysis of the overall financial position of Edmonton Airports to determine its general financial position and its ability to fund capital requirements for the system. The financial review concludes with an analysis of the City Centre Airport's projected financial position by reviewing its 10-year budget forecast and the related assumptions.

Financial Statement Analysis

Revenues: Operation of the City Centre Airport accounts for approximately 3% of Edmonton Airports' revenue stream. The City Centre Airport generates revenues from airside fees (59%) and commercial activity (41%). Airside revenues are composed of primarily the airport user fee, landing fee, and aircraft parking; commercial revenues consist primarily of land and hangar rentals. The City Centre Airport revenues in 2002 were up by \$0.2 million over 2001 to \$2.2 million. The primary factor in this increase was the rise in the airport user fee, from \$4 per landed seat in 2001 to \$6 in 2002. The

rate was increased to \$10 per landed seat in 2003. It is too early to determine the full impact of that change on revenues.

The OCA survey results indicated that further increases in rates and fees may not be a viable source of increased revenue. As a result, Edmonton Airports needs to evaluate how further increases would impact activity at the airport. In addition, it should continue to explore other revenue sources.

Expenses: The City Centre Airport accounts for approximately 4% of Edmonton Airports' operating expenses. The City Centre Airport's operating expenses in 2002 were up \$0.4 million over 2001 to \$2.7 million. The majority of the operating expense is fixed, due to Edmonton Airports' contract with a service provider for administrative and operations services at the City Centre Airport (\$1.6 million in 2002). The non-operating expenses including depreciation and interest expenses, which totalled \$667,000 in 2002, are directly correlated with the planned capital program. As a result, there are few opportunities to reduce total operating expenses under the current operating assumptions.

Total expenses (including depreciation and interest expenses) at both Edmonton Airports as a whole and the City Centre Airport have been higher than revenues for the past two years. However, Edmonton Airports as a whole and the City Centre Airport forecast small overall surpluses for 2003.

Net Earnings: The City Centre Airport has been in a net loss position since 1997, the first full year of consolidation, ranging from \$1.3 million in 1997 to \$266,000 in 2001 and \$515,000 in 2002 (see Figure 2). Much of the net loss is attributable to high depreciation expenses. The City Centre Airport has, however, experienced positive net earnings of approximately \$120,000 in the first half of 2003 (not depicted in Figure 2).

Figure 2

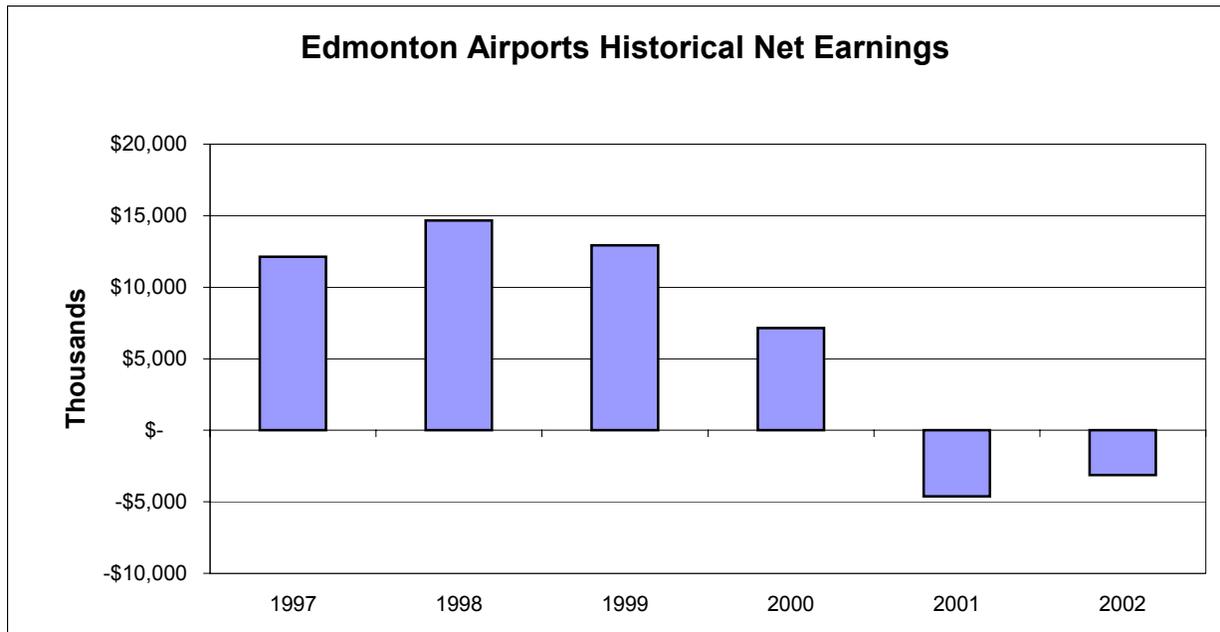


Not all expenses associated with the City Centre Airport are identified in its financial statements and, as a result, are not reflected in its net earnings. These expenses are provided by Edmonton Airports corporately and are mainly for administrative services (e.g., finance, human resources, legal, consulting, monitoring compliance with the passenger cap, and marketing). In the 2003 budget, there was an allocation to the City Centre Airport that reflected its share of the costs of the strategic study, indicating a step toward addressing full cost allocation at the City Centre Airport. Without full cost allocation, it is not possible for Edmonton Airports to determine the true cost of operating the City Centre Airport. The result is that the City Centre Airport net earnings

are overstated by an unknown amount (i.e., the actual net losses are greater than shown).

Edmonton Airports has also experienced a net loss over each of the past two years (see Figure 3). Prior to 2001, Edmonton Airports generated positive net earnings and the current net losses are the result of interest and amortization related to the \$300 million renovation and expansion underway at the International Airport. Edmonton Airports forecasts a return to positive earnings in 2003, with a continuing upward trend over time as interest expense declines and revenues increase.

Figure 3



In 2003, presentations were made to Council from interested stakeholders voicing their concerns regarding the future of the City Centre Airport. Concern was also raised regarding the financial health of the airport industry and specifically that of Edmonton Airports. Some of those concerns were that Edmonton Airports is losing money and is operating at a deficit.

The OCA followed up on those concerns by doing a comparison of Edmonton Airports' net earnings with other major airport authorities across Canada. The airports chosen were Winnipeg, Ottawa, Halifax, Calgary, and Vancouver. In this analysis, Edmonton Airports was found to be the only airport authority with negative net earnings during 2001 and 2002. The OCA based its analysis on audited financial reports and passenger statistics that were publicly available. The OCA recognizes that comparisons across airports are difficult due to differing sizes of airports and different stages and scope of capital development.

Cash Flow: Cash flow is the net cash flow from operations. It is calculated from the income statement by adding back non-cash items such as depreciation. Cash flow is a measure of short-term viability and the ability to service debt. The OCA financial analysis of City Centre Airport indicates that given the airport's current financial situation, it is unable to finance its capital investment from its cash flows.

Short and Long-term Debt: The OCA calculated financial ratios that indicate an organization's ability to access cash or near cash financial instruments to meet its current liabilities. Current ratios are the proportion of cash and near cash assets (marketable securities, receivables, inventory, etc.) compared to current liabilities (payable within one year). Current ratios greater than one are desirable, indicating that there is sufficient cash and near cash available to cover short-term liabilities.

Edmonton Airports has had reasonable current ratios for the past two years and is showing a current ratio of 2.0 for the first six months of 2003. The City Centre Airport has had generally strong current ratios for the past several years and is showing a ratio of 8.6 for the first six months of 2003. This means that both Edmonton Airports and the City Centre Airport are currently able to meet their short-term obligations.

Long-term debt is composed of liabilities that are payable over a term of greater than one year. In the 2002 financial statements, Edmonton Airports reported \$249 million in long-term debt (primarily 30-year 'Series A' bonds) including \$4.4 million at the City Centre Airport. This debt is being used primarily for funding of the Air Terminal Redevelopment Project at the International Airport.

Edmonton Airports is carrying that indebtedness at an interest rate of about 7.21% which is comparable to the interest paid by other Canadian airport authorities for their 30-year term debts. According to the Dominion Bond Rating Service rating scale, Edmonton Airports' A-High rating is considered 'Investment Grade' and reflects a high level of comfort with the airport's overall credit quality. The rating indicates that Edmonton Airports has a strong ability to repay interest and principal under normal conditions but may be somewhat vulnerable to adverse economic conditions.

10-Year Budget Forecast

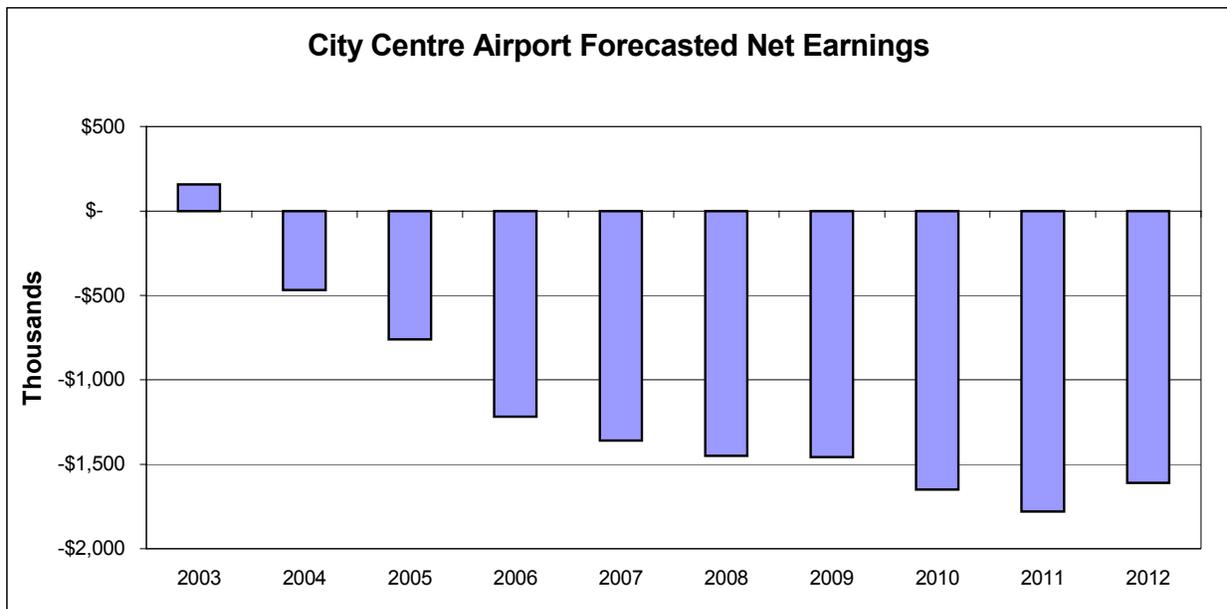
The final iteration of the Edmonton Airports' 10-year budget forecast for the City Centre Airport for the period 2003 to 2012 was made available to the OCA on September 22, 2003.

The OCA reviewed the financial projections and assumptions contained in the forecast and found the assumptions used for inflation, escalation of capital costs, revenues, and expenses to be generally reasonable. The forecast is based on the January 1, 2004, airport access policy that restricts scheduled service to 10-seat aircraft and prohibits dedicated cargo, and assumes that it will remain in effect for the forecasted period. It also reflects the increasing capital expenditures programmed over the next ten years for the maintenance, rehabilitation and replacement of City Centre Airport infrastructure. As a result of the escalation in capital expenditures, forecasted depreciation and interest

expenses increase correspondingly over the next ten years, from approximately 20% of expenses in 2003 to over 50% in 2012.

Edmonton Airports' projections for the period 2003 to 2012 indicate that operating earnings (earnings before subtracting non-operating expenses such as interest and depreciation) at the City Centre Airport are expected to increase steadily from 2004 onward. The OCA believes that these projections are based upon reasonable assumptions. However, given the anticipated capital expenditure program, the impact of the related depreciation and interest expenses will create negative net earnings from 2004 (approximately \$467,000) through 2012 (approximately \$1.6 million), as is illustrated in Figure 4.

Figure 4



D. Business Development

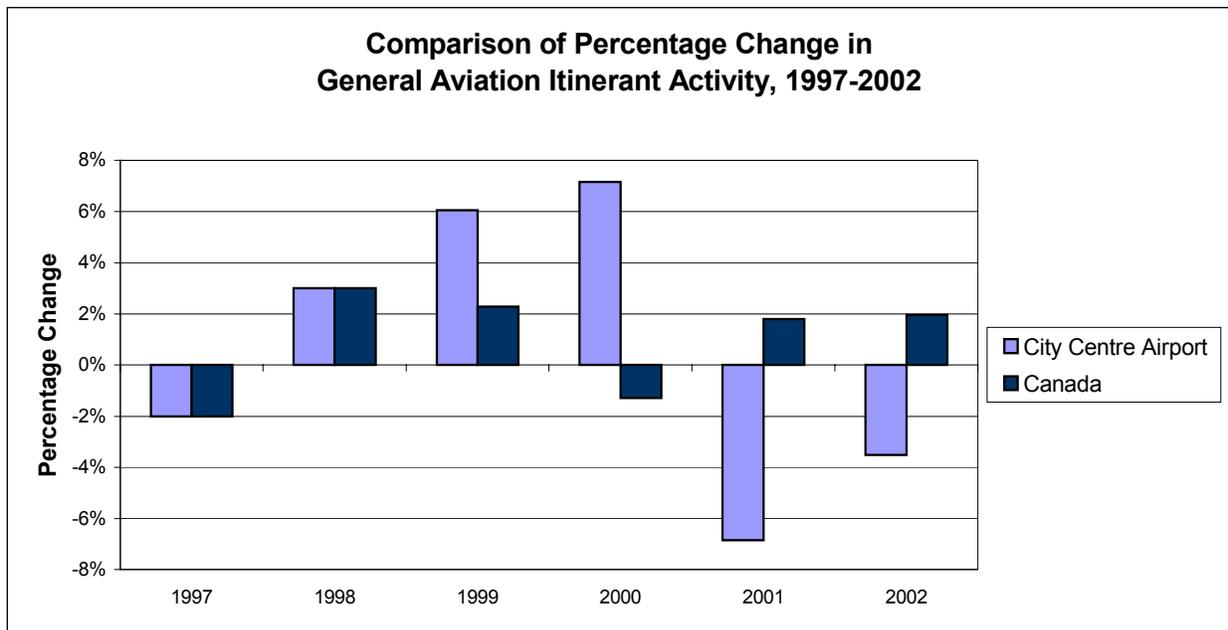
The OCA reviewed both aviation and non-aviation business development at the City Centre Airport, using Edmonton Airports’ 1995 five-year strategic plan, *Airports 2000*, as the reference against which to measure progress. Edmonton Airports’ business development activities were also examined from the perspectives of rates and fees charged to users, general marketing of the City Centre Airport, and communications with tenants and other stakeholders.

Aviation Business Development

The amount of general aviation activity at the City Centre Airport has increased since 1997, the first full year of consolidation. During the first few years, its growth matched or exceeded that of Canada overall.¹⁵ However, activity at the City Centre Airport declined in 2001 and 2002 while growth continued elsewhere in Canada, as is illustrated in Figure 5. That period coincided with an increase in fees at the City Centre Airport after several years of little or no fee increases (see “Rates and Fees” section that follows).

¹⁵ Transport Canada Aviation Forecasts, 2002-2016

Figure 5



In the 1995 strategic plan, Edmonton Airports saw the City Centre Airport fulfilling three primary roles as a general aviation airport: corporate aviation, utility general aviation, as well as aerospace manufacturing and aviation support services. No scheduled service was envisioned as remaining at the City Centre Airport post-consolidation, although a portion of scheduled air service remains at the airport today.

Corporate Aviation: The International Business Aviation Council defines corporate aviation as “aircraft transport operation on behalf of a company, other than commercial

air transportation, in connection with the transport of passengers or cargo for that company.”

The activities planned to build this role, as listed in the 1995 business plan¹⁶, included involving current corporate aviation tenants in a consultation process regarding the following:

- The strategic direction of the airport;
- The development plans for the airport;
- The services to be provided and facilities to be supported;
- The efforts to balance costs and services to minimize fee increases; and
- Future capital investment plans.

In 1996, the City Centre Airport’s business plan envisioned the City Centre Airport becoming, over time, a ‘Centre of Excellence for Corporate and General Aviation’ – a one-stop centre where owners and operators of corporate and general aviation aircraft could obtain a full range of maintenance, overhaul, and other support services.

Between 1996 and 2000, Edmonton Airports attended Canadian Business Aviation Association and National Business Aviation Association conventions. In 2000, Edmonton Airports commissioned a study to strategically position the City Centre Airport as a corporate aviation airport. The report was completed in 2001¹⁷ and preliminary efforts to position the City Centre Airport as a corporate aviation airport were initiated in 2002. These efforts were suspended in the fall of 2002 as Edmonton Airports’ concern regarding financing capital expenditures and legal challenges increased.

The OCA’s survey indicated that 82% of respondents rated Edmonton Airports’ efforts “to develop increased use of the City Centre Airport by corporate aviation and activities related to corporate aviation” as poor. In part, the response may be a reflection of the frustration respondents feel regarding the suspension of the market positioning efforts.

Utility General Aviation:¹⁸ According to the 1995 strategic plan, this role was to encompass charter flights, medevac flights, military aerial survey, aerial spraying, forest fire suppression, light cargo and aviation education.

In the 1995 strategic plan, Edmonton Airports committed to the following:

- Developing marketing materials with input from tenants;
- Supporting major users in staging awareness day(s) targeted to defined potential clients;

¹⁶ *Edmonton Airports Strategic Plan: Airports 2000* (1995), Appendix B, p. 21

¹⁷ *Edmonton City Centre Airport 2001 Report: Developing a Perception of High Value* (2001), prepared for the Edmonton Regional Airport Authority by Focal Customer Development Inc.

¹⁸ By definition, “utility” general aviation is more commonly referred to as “business” aviation.

- Attending trade shows to promote tenant facilities and services as well as to attract new business;
- Developing an incentive program to attract new tenants and encourage existing tenants to expand; and
- Investigating the interest for a co-operative advertising program.

Edmonton Airports made reasonable efforts to implement these objectives. Marketing activities involved publishing tenant directories, advertising in aviation business directories, attending and hosting Canadian Owners and Pilots Association conventions, and sponsoring Airfest, an aviation festival, beginning in 1998. The development incentive program ran from 1997 to 1999 and provided financial incentives for eligible capital projects involving the construction of new tenant facilities and the expansion or renovation of existing facilities. Edmonton Airports also developed a corporate web site in 2000 that included information on its four airports.

Aerospace Manufacturing and Aviation Support Services: In its 1995 strategic plan, Edmonton Airports recognized that efforts to attract aerospace manufacturing would need to be considered long-term in nature and was willing to invest “significant efforts in both terms of time and financial resources.”¹⁹

In the first few years post-consolidation, efforts were made to attract businesses in the aerospace industry to invest in operations at the City Centre Airport. From 1996 to 1998, Edmonton Airports, the Northern Alberta Institute of Technology, and the University of Alberta also worked to establish an aerospace/aviation training centre at the City Centre Airport, but they were unsuccessful.

Edmonton Airports expected that the synergies created from offering a full range of maintenance, overhaul, and other support services at the City Centre Airport would enable the airport “to attract businesses and customers from other airports and prosper, even if there was no overall growth in the local corporate and general aviation community.”²⁰

The OCA survey confirmed that a variety of aviation operations are based at the City Centre Airport. However, 88% of the OCA-survey respondents rated Edmonton Airports’ efforts “to attract aerospace and aviation-related industries” as poor. A plan does not currently exist that clearly outlines general aviation business development among Edmonton Airports’ four airports. The strategic study being undertaken by Edmonton Airports in 2003 may address this need.

Non-Aviation Business Development

Airports commonly lease lands surplus to aviation needs in order to generate additional revenues and keep aviation-related fees lower. In the 1995 strategic plan, Edmonton Airports acknowledged that it, too, would explore non-aviation land uses for parcels of land that were “less attractive/suitable” for aviation purposes and that one of its

¹⁹ *Edmonton Airports Strategic Plan: Airports 2000* (1995), Appendix B, p. 23.

²⁰ *Edmonton City Centre Airport 1996 Business Plan*, p. 7.

marketing priorities would be “broadening the scope of the airport to attract non-aviation-related business to airport property.”²¹

Participants in the OCA survey were asked to evaluate Edmonton Airports’ efforts toward meeting this marketing priority and responded in this manner:

- 21% of respondents rated Edmonton Airports’ efforts as “very good.”
- 32% of respondents rated Edmonton Airports’ efforts as “good.”
- 13% and 17% of respondents rated Edmonton Airports’ efforts as “fair” or “poor.”

When asked to provide further comments, 68% of respondents stated they felt that the non-aviation activity was at the expense of aviation activity.

With limited growth in the general aviation industry, Edmonton Airports struggled from 1996 to 1998 to find aviation tenants for the land that is now occupied by non-aviation development. In the spring of 1999, City Council approved the rezoning of select sections of airport lands to allow specific non-aviation uses (commercial and light industrial). It was only after the rezoning of some of the airport lands to allow non-aviation uses that Edmonton Airports was able to find tenants.

Although three of the four non-aviation developments at the City Centre Airport are located on sites that were formerly committed to aviation land uses, including the former passenger terminal building, they are in accordance with zoning. The City reviewed and approved these land leases in accordance with article 25 of the lease.

Currently, Edmonton Airports limits non-aviation business development to no more than 30% of total development at the City Centre Airport (which is the equivalent of 8% of the total airport lands). It assesses the suitability of proposed developments on a case-by-case basis as opportunities arise and in accordance with zoning requirements.

According to the *City Centre Airport 2002 Annual Review* submitted by Edmonton Airports to the City, aviation development stalled when the issues surrounding the future of the City Centre Airport created sufficient uncertainty to discourage real estate development. Edmonton Airports may also be unwittingly feeding the uncertainty, as is demonstrated by a December 20, 2002, letter from Edmonton Airports to the City Manager:

Edmonton Airports is prepared to proceed with commercial aviation developments provided that the lease terms reflect the current business climate at [the City Centre Airport]. Edmonton Airports is not prepared to accept any liability for new developments that are dependent on the continued operation of the airport. This risk would have to be assumed by the developer of the project.

²¹ *Edmonton Airports Strategic Plan: Airports 2000* (1995), p. 12.

Such sentiments, combined with fee increases and changing access policies, likely serve to heighten the longstanding uncertainty that persists at the City Centre Airport. Overall development at the airport could be enhanced through the creation of a detailed master plan. A master plan identifies and evaluates airport development alternatives that satisfy future aviation-related demand, are responsive to the needs of the airport and the community, and maximize revenue-generating opportunities while effectively managing land uses.

Rates and Fees

Edmonton Airports has long-recognized that the general aviation activity at the City Centre Airport did not generate sufficient revenue to support its infrastructure and facilities. Nonetheless, it committed in the 1995 strategic plan to keeping rates the same for three years post-consolidation.²² The belief was that raising fees and land lease rates was not an attractive option to increase revenues because it would depress aviation activity and lead the City Centre Airport away from its vision, rather than toward it.²³

In 2001, Edmonton Airports increased the landing and user fees to meet Edmonton Airports' objective of eliminating the operating deficit within a five-year timeframe. More frequent rate increases followed as the goal changed from eliminating the operating deficit to reducing the capital deficit. With the exception of the airport user fee, the rate increases brought the fees in line with other airports. However, the rapidity and degree of the rate increases posed a challenge for the airport businesses.

In 2002, landing and user fees combined comprised 55% of the City Centre Airport revenues, which is comparable to the proportion of fees prior to consolidation. For 2003, this revenue is expected to increase to 67%, due largely to a March 1, 2003, rate increase that saw the landing fee rise by 13% and the user fee rise by 67% from the September 2002 levels. The land lease rates have also increased recently, but the added revenue will be realized as leases are renewed.

The 2003 Edmonton Airports' corporate business plan notes that the fee increases send an "unmistakable message to users that they will be put on an incremental path to pay for the fully allocable costs, both operating and capital, of using the airport."²⁴ Coupled with Access Policy changes limiting the type of aircraft allowed for scheduled passenger service and eliminating dedicated cargo operations, fees will likely continue to rise as costs are spread over fewer users.

The OCA survey results indicated that 10% of respondents believe that City Centre Airport's current fee levels are reasonable for the services and facilities provided at the airport and relative to fees charged at other airports. Of the remaining respondents, 62% did not feel the fees were reasonable and 28% did not know or were uncertain.

²² *Edmonton Airports Strategic Plan: Airports 2000* (1995), p. 19.

²³ *A Vision for Edmonton City Centre Airport* presentation package for Edmonton City Council, dated April 15, 1998, p.6.

²⁴ *2003 Edmonton Airport Business Plan*, p.13 of the Executive Summary.

When asked if businesses would be willing to pay higher fees to maintain the status quo at the airport, 21% of respondents were willing to pay higher fees, 56% were not and 23% did not know.

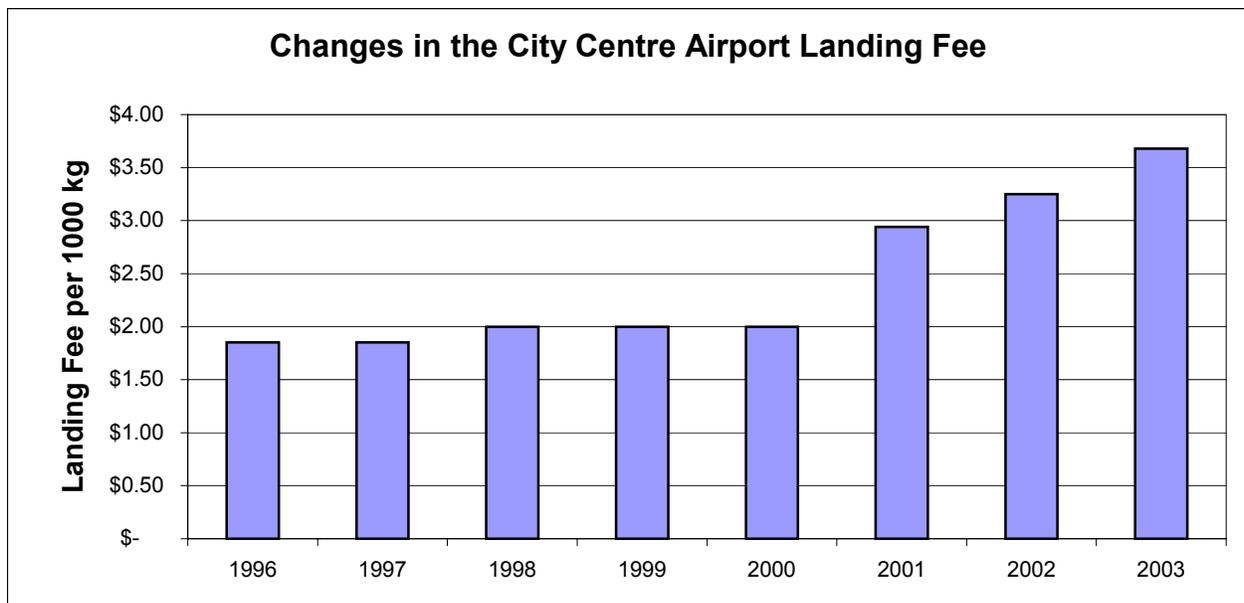
The historical changes in the aviation fees and land lease rates are discussed in greater detail below.

Landing Fee: The City Centre Airport assesses aircraft landing fees of \$3.68 per 1000 kg per landing with a \$12 minimum charge per landing. However, flight schools and locally based private operators pay a nominal annual rate.

Prior to Edmonton Airports assuming management of the airport, the landing fee was \$1.85 per 1000 kg per landing. The rate rose to \$2.00 in 1998. Edmonton Airports anticipated that further increases of rates and fees would be necessary to contribute to the financial stability of the airport. However, the 1998 Annual Review indicated that Edmonton Airports deemed that an immediate increase was unnecessary, given the City Centre Airport was on schedule with its 5-year deficit reduction plan.

In 2001, the landing fee increased from \$2.00 to \$2.94 per 1000 kg, a 47% increase, and more frequent rate increases followed, as is highlighted in Figure 6. Overall, the landing fee rate has increased by 99% since consolidation. It is important to note that the rate is now the same as that at the International Airport, which is within the normal range for international airports. The fee is higher than some Alberta general aviation airports; however, the City Centre Airport may command a premium rate by virtue of its downtown location.

Figure 6



Airport User Fee: The purpose of the airport user fee is to assist the City Centre Airport with meeting all of its costs, including capital. This fee was introduced by the City of Edmonton and has always represented a significant source of revenue. In 1995 (prior to consolidation), revenues from the user fee represented 44% of all revenues. That proportion decreased to 38% by 2002, but is expected to increase to 46% in 2003 with the March 2003 rate change.

The airport user fee of \$10 per landed seat applies to all aviation operations “including private, charter, rotary wing, government and military use and applies to all aircraft with landed seats of four or more” if no waiver of the fee has been provided by Edmonton Airports. For charter and cargo operations, the user fee is charged based on the capacity of the aircraft (e.g., \$100 for a 10-seat aircraft, \$190 for a 19-seat aircraft); for scheduled air services, it is charged based on the 10-passenger cap (i.e., to a maximum of \$100 per landing).²⁵

The airport user fee has increased dramatically over the past two years, from \$4 per landed seat in July of 2001 to the current rate of \$10 per landed seat. The 150% increase was deemed necessary to permit the progressive recovery of historical capital investment at the airport and to fund future capital requirements. This fee is unique to Edmonton’s system of airports and dramatically increases the cost of doing business here.

The OCA conducted a survey of the standard rates and fees levied at various airports in Alberta, Saskatchewan and Manitoba. The cost of landing a 19-seater charter or cargo flight at the City Centre Airport is, on average, nine times as costly (\$216 versus an average of \$24) compared to the other airports surveyed.²⁶ The cost of landing a scheduled passenger flight at the City Centre Airport is, on average, more than twice that of the other airports (\$126 versus an average of \$55).²⁷

In contrast, the International Airport levies a “landed seat” fee of \$6 (compared to the City Centre Airport’s user fee of \$10 per landed seat) for general aviation flights on fixed wing aircraft with a seating capacity of 5 or more seats. The fee is not levied against small cargo operations, but would be levied against small charter flights. Therefore, the landing and user/landed seat fees charged to operate a 19-seat charter aircraft from the International Airport would total approximately \$140, compared to \$216 at the City Centre Airport. Cargo operations, exempt from the International’s landed seat fee, would pay approximately \$26 in landing fees compared to \$216 in landing and user fees at the City Centre Airport.

Land Lease Rate: In 2002, Edmonton Airports completed a review of land market values and increased its land lease rate from \$2.75 to \$3.48 per sq. meter (an increase of 27%) for new tenants or renewing tenants who do not have a lease rate escalation clause in their lease agreement. This was the first increase since consolidation and was intended to bring the rates in line with the market. The 2002 lease rates will be in effect until Edmonton Airports undertakes its next market value assessment in 2007.

²⁵ When the City operated the airport, it charged a user fee of \$5.30 per enplaning and deplaning passenger to generate sufficient operating and capital funds to operate the airport. Edmonton Airports modified the application of the fee in 2001 to apply to deplaning passengers only.

²⁶ The assumption is that the aircraft is operating from a fixed based operator instead of a terminal. As a result, terminal and airport improvement fees are not included in the calculation.

²⁷ For scheduled services, the fees for the other airports generally include a terminal fee in addition to the landing fee. No terminal fee is assessed at the City Centre Airport, only landing and user fees.

Marketing

Marketing helps a corporation achieve its strategic objectives and should therefore flow from the business strategy. Edmonton Airports' 1995 strategic plan included a high-level marketing plan for the City Centre Airport. It included long-term objectives and some major marketing strategies to be used to attain them. It did not identify the resources required to execute these strategies nor anticipated time-lines.

In 1996, Edmonton Airports identified the need for a three-year marketing plan for the City Centre Airport and it appears as a recurring objective thereafter. Several steps were taken between 2000 and 2002²⁸ to bring Edmonton Airports closer to producing a long-range City Centre Airport marketing plan, but further efforts were placed on hold as uncertainty concerning the future of the airport increased.

Edmonton Airports has asserted that it has invested significant resources in promoting the City Centre Airport. However, the financial data do not fully disclose the level of investment because of the limited allocation of costs to the City Centre Airport. As was reviewed earlier in this report, there is evidence of the promotion of the City Centre Airport in aviation directories, at aviation trade shows and conventions, and through brochures, information sheets, the Edmonton Airports web site and the development incentive program. The longstanding uncertainty regarding the City Centre Airport's future may limit the effectiveness of any marketing program that Edmonton Airports may choose to adopt.

The OCA's tenant survey indicated that 72% of respondents rated Edmonton Airports' efforts to "work closely with current tenants to develop joint marketing, advertising and promotion plans" as poor. The timing of the survey may have magnified respondents' ratings, but the perception of tenants remains an important issue for Edmonton Airports to address.

Communications

Strong communications keep parties focussed on goals and priorities while providing feedback on progress and any needed course corrections. The methods that Edmonton Airports has used to communicate with stakeholders are discussed below.

Tenants' Association: Edmonton Airports' first stated priority after consolidation was to work with tenants to help them succeed, recognizing that "successful and supportive tenants can become a sizeable, motivated and effective sales team working with Edmonton Airports" to re-position the airport²⁹. Edmonton Airports anticipated that a tenants' association could serve to provide input into an Edmonton Airports' marketing plan and participate in implementing the resulting marketing initiatives. However, the Tenants Association reportedly did not believe that Edmonton Airports was receptive to the association's input and the relationship became very strained. The last time the Tenants Association provided input was during the rezoning debate in 1998.

²⁸ *Edmonton City Centre Airport 2001 Report: Developing a Perception of High Value* (2001), prepared for the Edmonton Regional Airport Authority by Focal Customer Development Inc.

²⁹ Edmonton City Centre Airport 1996 Business Plan, p. 6.

Newsletter: In 1998, Edmonton Airports created a newsletter to provide information to tenants and invited tenants to provide news items as well. The newsletter was active from 1998 to 2000, but was suspended while resources were dedicated to a market positioning study. There were plans to re-start the newsletter in 2002, but this effort was placed on hold as uncertainty concerning the City Centre Airport's future grew.

Advisory Committee: One of Edmonton Airports' major objectives for 1996 was to create an external advisory body that would provide broader perspectives on issues affecting the development of the City Centre Airport and to assist in disseminating information to broader markets. The Advisory Committee was created in 1997 and was comprised of tenants and other stakeholders including Ward 2 Councillors, representatives from surrounding residential communities, representatives from Transport Canada, NAVCAN, and Air Traffic Control. Meetings occurred infrequently and, by 2001, the committee had ceased meeting altogether.

Marketing Committee: The Marketing Committee was developed to identify and build stakeholder relations (internal and external), to develop and implement a marketing program and business plan. To ensure the committee remained active and viable, Edmonton Airports was to establish means to measure and report upon the Marketing Committee's success. The committee, comprised of the spectrum of airport and aviation businesses at the City Centre Airport and the Edmonton business community (e.g., Kingsway Business Association), met throughout most of 2002. In the fall of 2002, Edmonton Airports placed the committee "on hold" as it determined the future of the airport. The OCA's survey found that 67% of respondents rated the effectiveness of the Marketing Committee in marketing the City Centre Airport as "poor" and 29% indicated they were not familiar enough with the initiative to provide a rating.

Business Development Office: The Business Development Office was opened on City Centre Airport land in 2002. The purpose of the office was to function as a liaison point for City Centre Airport stakeholders and tenants and the Marketing Committee, improve the coordination of the marketing plan's implementation, and improve the accessibility of Edmonton Airports' staff to City Centre Airport tenants and the local business community. With the suspension of many of the City Centre Airport marketing activities, the office is now open primarily when the Manager of General Aviation Services and other Edmonton Airport staff need to transact business at the City Centre Airport. This can range from twice per week to infrequently. The OCA's survey found that 68% of respondents rated the effectiveness of the Business Development Office in marketing the City Centre Airport as "poor" and an additional 28% indicated they were not familiar enough with the initiative to provide a rating.

Stakeholder Relations Survey: Edmonton Airports annually commissions stakeholder surveys to evaluate Edmonton Airports' success in meeting its stakeholder and community relations goals. Participants include provincial and municipal governments, business and community leaders as well as Edmonton Airports' tenants and business partners. In 2002, the survey results acknowledged that there are diverse opinions

among stakeholders as to the preferred future use of the City Centre Airport and that there was little chance of ever obtaining consensus. The stakeholder survey respondents rated improved relations with the City Centre Airport tenants as one of the areas requiring improvement, which is consistent with the results of the OCA survey.

Business Plans: The Lease requires that Edmonton Airports present the City Centre Airport's business plan, a review of the business plan results, and financial information at annual public meetings. However, the information contained in these documents has had generally a shorter-term focus, as noted in the Lease Compliance section of this report. Edmonton Airports needs to provide stakeholders with its long-term vision for the airport to allow stakeholders to plan accordingly and is in the process of creating a new strategic plan to address this need.

Respondents to the OCA's survey were asked to evaluate Edmonton Airports' communication of its business initiatives concerning the City Centre Airport. The majority of the respondents felt that Edmonton Airports did not regularly communicate initiatives to them by newsletters, email or information meetings. A portion of respondents felt that the primary means of hearing about initiatives was through word of mouth, gossip or the media. Roughly one-third of survey respondents rated Edmonton Airports' accessibility through phone, email or in-person as good to very good, one-third rated it as poor to fair, and one-third did not know or were uncertain.

If Edmonton Airports' vision for the City Centre Airport is unclear or not communicated clearly, tenants are unable to strategically position themselves. The uncertainty surrounding the airport and the frustration felt by some stakeholders, particularly the tenants, may demonstrate its impact through reduced investment, further reinforcing the perception that the airport's long-term future is in question. Edmonton Airports states that its strategic study is intended to address the issue of uncertainty at the City Centre Airport.

E. Economic Impact Analysis

The OCA has examined the implications of planned and potential changes in airport access policies that could have material consequences to the City Centre Airport's financial situation and economic role and impacts. The policy changes assessed include the planned policy amendment that will take effect January 1, 2004, disallowing dedicated air cargo operations and restricting scheduled air passenger aircraft to those having a maximum capacity of 10 seats.

The economic impact analysis also examined the potential effects if all scheduled passenger services are restricted, given this was the proposal put forth in Edmonton Airports' 1995 strategic plan and the expectation of the majority of the voting public in the 1995 referendum. The lease also acknowledges that Edmonton Airports would be restricting scheduled air passenger service at the City Centre Airport.

The impact analyses carried out are relevant to the City given the current importance of the City Centre Airport to the Edmonton region and the potential effects of the potential access policies on the economic and financial "value" of the City-owned airport lands

and facilities. In undertaking the analyses, the primary vantage point taken has been the impacts on the City Centre Airport and the businesses located there. However, some consideration has been given as well to the possible effects on the International Airport and the northern communities served by the City Centre Airport. The scope of the research carried out has not included a review of the full costs and benefits of the policy changes to the regional airport system or the City's economy as a whole and the results should not be interpreted as representing the full impacts of the policy changes. The results of the impact analyses are documented in Appendix 2, with a brief summary of findings provided below.

Impacts of Planned Access Policy Amendment

The impacts of the January 1, 2004, access policy amendments on the City Centre Airport and the airport's associated business community are expected to be moderately negative, reducing current levels of airport revenue and economic activity in the order of 10%, which is consistent with the City Centre Airport's financial projections.

The most significant impacts are likely to stem from the heightened uncertainty and reduced confidence among businesses regarding the airport's prospects and the potential effects on their business intentions and future investments at that location. The modified access policy is likely to have a marginally positive financial effect on the International Airport. Edmonton Airports believes that the moderately negative impacts at the City Centre Airport will be more than offset by moderately positive impacts to the system.

Impacts of Removing Scheduled Passenger Services Access

The potential discontinuance of all scheduled passenger services at the City Centre Airport, consistent with the direction of the 1995 referendum, could have the effect of reducing the airport's current aircraft movements by 20% and the number of enplaned and deplaned passengers by more than 70%. The City Centre Airport's airside revenues may decline by an estimated \$1.2 million annually and the airport's land and hangar rental income could be affected through the loss of some aviation-related support businesses. Once again, heightened uncertainty and reduced confidence among businesses regarding the airport's prospects could intensify this effect. The City Centre Airport's total revenues could be expected to decline by more than 40%.

The net impacts on the airport's financial performance would depend on parallel management actions taken relating to operating and capital expenditures, fees and charges, and marketing and business development, and might be alleviated in some part by the growth in corporate and charter air traffic. As a result, Edmonton Airports challenges the OCA's conclusion that revenues would decrease by 40%, anticipating the impact to be closer to 25%.

The loss of scheduled services at the City Centre Airport would have varying degrees of impact on Fort McMurray, Fort Chipewyan, High Level, Grande Prairie, and Peace River, which could experience some reduced air service choice and competition. Many business travellers from the north prefer the access and convenience that the City

Centre Airport offers for conducting business in the city's downtown and a shift to the International Airport would infer some loss of convenience, extra travel time and, potentially, cost. However, the International Airport also serves the communities served by the City Centre Airport.

VIII. Summary Points

Based on a high-level review of the City Centre Airport's operating plan, including an assessment of current and projected financial positions, the reasonableness of identified infrastructure needs and projected funding sources and the investments in aviation, the OCA has the following findings:

1. In general, Edmonton Airports has been in compliance with the lease agreement.
2. The proposed capital program for the City Centre Airport that was presented by Edmonton Airports is reasonably justified as being required to maintain, rehabilitate or replace the existing infrastructure.

Without a fundamental change in infrastructure funding requirements, however, the OCA's analysis indicates that the City Centre Airport is unable to fund its capital program entirely from cash flow. Any changes to infrastructure capacity would directly impact the level of capital investment required to maintain the infrastructure.

3. Transport Canada concluded that the City Centre Airport met the applicable operating safety regulations and standards as required to continue airport operations.
4. The OCA's analysis confirms that operating earnings at the City Centre Airport for the period 2003 to 2012 should increase from 2004 onward given the assumptions used. However, the OCA recognizes that the impact of increasing depreciation and interest expenses resulting from the 2003-2012 capital plan will create negative net earnings from 2004 through 2012.
5. Net earnings have become a major issue for the City Centre Airport because of a change in funding philosophy by Edmonton Airports from a system capital funding perspective in 1995 to a user-pay perspective regarding operating and capital expenses.
6. The likely economic effect of the modified access policy (limiting scheduled air service to 10-seat aircraft and prohibiting dedicated cargo) to be implemented on January 1, 2004, would be to reduce City Centre Airport revenues by approximately 10%. This is consistent with Edmonton Airports' financial projections for the airport.

Changes to the access policy are within the authority of Edmonton Airports, providing they meet the requirements of the lease. The most significant impacts of the proposed policy changes are likely to stem from the heightened uncertainty and reduced confidence among businesses regarding the airport's prospects and the potential effects on their business intentions and future investments at that location.

7. All non-aviation developments are in accordance with zoning and were approved by the City. Overall development at the airport could be enhanced through the creation of a detailed master plan.
8. Edmonton Airports made reasonable efforts in implementing the marketing plan outlined in its 1995 strategic plan. Nonetheless, business development can be strengthened through a plan that clearly outlines general aviation business development among Edmonton Airports' four airports.
9. Edmonton Airports has undertaken a variety of initiatives to communicate with City Centre Airport stakeholders, with varying degrees of success and sustainability. The City Centre Airport continues to be challenged by the longstanding uncertainty concerning its role and its future.

The uncertainty manifests itself in the results of the OCA's survey, where Edmonton Airports' efforts to work with tenants and develop effective communication tools were rated as poor by a substantial majority of the respondents. The timing of the survey may have magnified respondents' ratings, but the perception of tenants remains an important issue for Edmonton Airports to address. Tenants remain unconvinced of Edmonton Airports' commitment to maintain aviation and aviation-related services at the City Centre Airport.

10. The airport user fee, which is used to fund operating and capital costs at the City Centre Airport, dramatically increases the cost for users of the City Centre Airport. A comparative study of airports indicates that the cost of operating charter and cargo services at the City Centre Airport is higher than at other airports. The City of Edmonton created the airport user fee when the airport was under its management and it continues to be a significant source of airport revenue.
11. Lack of clarity in Edmonton Airports' vision for the City Centre Airport or failure to communicate it clearly will affect the tenants' ability to strategically position themselves. The uncertainty surrounding the airport and the frustration felt by some stakeholders, particularly the tenants, may demonstrate its impact through reduced investment, further reinforcing the perception that the airport's long-term future is in question.

IX. Conclusion

Edmonton Airports' current goal for the City Centre Airport is financial self-sufficiency. Airport users will be required to pay for the fully allocated costs, both operating and capital, without any form of subsidy from the International Airport. Consequently, the City Centre Airport's financial challenge is to generate sufficient revenues to meet all current and future obligations including the lease requirement of maintaining the capital infrastructure.

The majority of the City Centre Airport's operating expenses is fixed and is provided by a contract service provider. In addition, non-operating expenses including depreciation and interest expenses are directly correlated with the planned capital program. As a

result, there are few opportunities to reduce total operating expenses under the current operating assumptions.

In response to the financial challenge of generating sufficient revenue, rates and fees have increased significantly. Coupled with pending access policy changes planned in January 2004, it is reasonable to expect that rates and fees will continue to rise as costs are spread over fewer users. One emerging strategy for generating additional revenue is to pursue land development. However, the development of prime aviation land for non-aviation purposes can have long term implications for future development at the City Centre Airport unless guided by an appropriate land-use master plan.

Edmonton Airports, in consultation with the community at large, must articulate a vision for the City Centre Airport that clearly defines its role within the current system of airports and has undertaken a strategic study with this stated purpose. The uncertainty surrounding the airport has resulted in the long-term future of the City Centre Airport being put into question. However, through the development of effective and actionable plans, coupled with effective consultation and communication strategies, the operation of the City Centre Airport will continue to benefit the City, Region, and Province.

X. Project Personnel

City Auditor: *David Wiun*

Audit Director: *Bill Cook*

Project Leader: *Gordon M. Babey*

Audit Coordinators: *Carol Ann Kushlyk*
Lisa Nykolyshyn

Economic Consultant: *Nichols Applied Management*

XI. Appendices

Appendix 1: Evolution of Edmonton Airports' Funding Philosophy Toward the City Centre Airport

Source Document	Statement Made (As Quoted)
Edmonton Airports Strategic Plan AIRPORTS 2000 (1995)	"Guiding Principle: Capital investment at all airports will be the responsibility of Edmonton Airports and will be treated as a system investment of Edmonton Airports."
Edmonton Airports Strategic Plan AIRPORTS 2000: Municipal Airport Business Plan (1995)	"Financial Feasibility: In each scenario the City Centre Airport is in a negative cash position in the year 2000 as the forecast capital requirements are in excess of annual operating cash flows. However, this is not a significant issue as one of the core principles of Edmonton Airports is that capital requirements are funded on a system basis. The airports as a system will generate sufficient cash flows to fund all capital requirements."
City Centre Airport 1997 Business Plan	"Business Development – To become #1 General & Corporate Aviation Airport in Canada. Financial – To be financially self-sustaining within five years. (The following Note was included: Financially self-sustaining is defined as a financial state whereby all operating costs associated with City Centre Airport are funded by airport revenues. Capital investment at all four Edmonton Airports will be treated as a system investment of Edmonton Airports.)"
City Centre Airport 2002 Business Plan	"The fee increase will be set at a level that, together with other revenue sources, permits City Centre Airport to meet all of its costs including capital, over the next 10 years."
City Centre Airport 2003 Business Plan	"During 2003 rates & charges will be amended to permit the progressive recovery of historical capital investment at the airport and to fund future capital requirements."
Edmonton Airports 2003 Business Plan	"At City Centre Airport users will be asked to pay more by way of rate increases to fund past and current capital expenditures. These rate increases, passenger access policy enforcement and the airports' role in the region's system of airports will be key issues."
Edmonton Airports 2003 Business Plan: Edmonton City Centre Airport	"These rate changes represent significant increases which combined with our clear policy on access sends an unmistakable message to users that they will be put on an incremental path to pay for the fully allocated costs, both operating and capital of using the airport."

Appendix 2: Economic Impact Analysis

The OCA has examined planned and potential changes in airport access policies relating to the City Centre Airport that could have material consequences to the airport's financial situation and economic role and impacts.

The most immediate policy change, planned to take effect January 1, 2004, will limit scheduled passenger aircraft to those having a capacity of 10 seats or less and disallow dedicated air cargo operations. The policy of allowing some level of scheduled air passenger service at the City Centre Airport was adopted in 1996 at the time of airport consolidation, and access provisions were subsequently adjusted to permit the use of 19-seat aircraft having a maximum load of 10 passengers. The planned access changes will allow scheduled passenger services to continue at the Airport, but under the same restrictions that were in place in 1996. Edmonton Airports is encouraging operators with larger aircraft to utilize the International Airport, where facilities are now in place that can accommodate these regional aircraft.

The referendum held in 1995 approved consolidation of scheduled air passenger services at the International Airport. Therefore, the potential exclusion of the remaining air scheduled services at the City Centre Airport is within the authority of Edmonton Airports under its management lease with the City. And clearly, any policy that allows scheduled services to remain at the City Centre Airport is contentious among those major airlines operating from the International Airport. The uncertainties surrounding the continuation of the current policy are reflected in the ongoing concerns and plans of businesses and operators at the City Centre Airport who fear that scheduled services could be restricted entirely at some time in the future.

The summary analyses that follow focus on the potential impacts that might arise from each of these two access policy changes. Particular reference is given to the effects on the City Centre Airport and its associated business community but some discussion of the implications to the International Airport and to communities in the north is provided as well. It is beyond the scope of the OCA's review to assess the full costs and benefits of these access changes to the regional airport system or to the city's economy as a whole, or to quantify the net effects that might accrue from parallel initiatives that might be taken by Edmonton Airports to mitigate any adverse impacts at the City Centre Airport. Accordingly, the analyses provided do not purport to advise as to the overall or net impacts and merits of the planned and potential policy changes.

Planned Access Policy Amendments

In January 2004, a modified access policy for the City Centre Airport will take effect. The policy will restrict use of the airport by air cargo operations, including air courier services, and scheduled air passenger aircraft having a capacity exceeding 10 seats. The modified policy will directly affect three scheduled air passenger operators that currently utilize 19-seat aircraft for flights to and from Calgary, Fort McMurray/Fort

Chipewyan, and High Level, and regular cargo operations that serve UPS, Purolator, and Bankers Dispatch.

The planned access changes directly affect air services encompassing 13% of the City Centre Airport's aircraft movements and about one-half of total enplaned and deplaned passengers but the ultimate impacts of the modified policy in terms of reduced aviation activity at the airport will depend on:

- The decisions taken by the existing scheduled airlines to discontinue or curtail services at the City Centre Airport, possibly shifting some services to the International Airport, or to convert to the use of smaller 10-seat aircraft at City Centre;
- Possible actions taken by other potential operators to introduce new services at the City Centre Airport with 10-seat aircraft;
- The potential shift of some business passengers to the use of charter or corporate aircraft; and,
- Passenger preparedness to travel on the smaller aircraft permitted under the modified access rules within the context of perceived safety and comfort factors.

The expected impacts of the modified access policy are summarized below.

City Centre Airport Traffic and Revenues: It is expected that under the planned access policy changes, dedicated air cargo services will consolidate at the International Airport and scheduled passenger traffic will decline by approximately 15-21%. This assumes that existing or new carriers will provide services to and from Calgary in smaller 10-seat aircraft, but that lower passenger acceptance of the smaller aircraft and some reduced travel flexibility will adversely affect overall passenger levels.³⁰ Some loss of traffic on other routes served by 19-seat aircraft is also assumed, as affected airlines adjust their fleets and some passengers shift to carriers offering larger aircraft. The particular responses of the various scheduled operators will of course affect the ultimate impacts on passenger activity.

The overall effect of the modified access policy would likely be to reduce overall passenger volumes (which includes scheduled, chartered and corporate traffic) at the City Centre Airport by an estimated 10%-14%, lower the number of aircraft movements by 5%-6%, and reduce airport revenues by approximately 10%. This is consistent with Edmonton Airports' financial forecasts.

Airport Business Community: The planned access policy changes will have a direct impact on affected air cargo and scheduled passenger operators. The former will need

³⁰ The perceived comfort and safety impacts on continued air travel at the City Centre Airport are uncertain. Most respondents to the WesTrends survey indicate that they may switch to other travel modes instead of using 10-seat aircraft. In contrast, most respondents (95%) to the recent Edmonton Airports passenger intercept survey expect to continue using the City Centre Airport once services are limited to 10-seat aircraft.

to relocate their operations from the City Centre Airport, the latter will need to modify their aircraft fleets and possibly adjust their routings and schedules.

The planned restrictions on the use of 19-seat aircraft will have the effect of reducing the perceived comfort and safety of scheduled air passengers and may result in some loss of air services at the City Centre Airport. Those business travellers now using the City Centre Airport who may shift to private vehicles or to alternative air routings via the International Airport will incur some extra travel time, inconvenience and, potentially, extra costs.

The expected reduction in scheduled passenger activity arising from the access policy changes will imply some loss of revenues to aviation service and supply businesses at the City Centre Airport and will have a negative impact on the general commercial vitality of the airport business community. The curtailment of growth prospects signaled by the modified access policy plus the possibly raised concerns about the outlook for continued scheduled passenger service are likely also to increase business uncertainty at the airport and affect aviation-related investment prospects. The possible loss or relocation of some existing businesses at the airport will detract from the agglomeration or “cluster” synergies that exist within the City Centre Airport business community.

The direct loss of employment that may arise from the modified access policy at the City Centre Airport is expected to be moderated because of the limited number of personnel engaged directly at the airport by the affected air cargo and scheduled passenger services. In the OCA survey of airport businesses, respondents forecasted that spin-off employment losses might total 110 to 120 positions, or about 8% of all aviation and non-aviation jobs at the City Centre Airport. This forecast could, in part, also reflect the impact of the tenants’ increased uncertainty concerning the future of the airport.

International Airport: The air cargo movement and a portion of the scheduled passenger activity that is diverted from the City Centre Airport through the modified access policy will accrue to the International Airport. However, a possibly larger share of the former passenger traffic at the City Centre Airport may shift to other modes, particularly vehicle transport.³¹ The Calgary traffic would be the most likely to switch modes, given Calgary’s close proximity³²; passengers to more distant destinations would likely continue to fly, whether on scheduled flights from the International Airport or on charter/private flights from either of the two airports.

Due to the lower activity levels and the dampened growth prospects at the City Centre Airport, some businesses might choose to relocate at or near the International Airport. The responses to the recent survey conducted by the OCA suggest, however, that a

³¹ In a recent survey of City Centre Airport passengers conducted by WesTrends Research, 22% of respondents indicated that if air services were further curtailed at the airport, they would reach their destination via the International Airport. By comparison, 51% reported that they likely would drive.

³² This is inconsistent with findings from the Edmonton Airports’ 2003 passenger intercept survey, which showed that 94% of Calgary passengers would use the 10-seat aircraft at the City Centre Airport, while 6% would travel by road.

greater proportion of relocating businesses might locate outside of the Edmonton region, to Calgary and other centres in Alberta and elsewhere in western Canada.

Northern Communities: The modified access policy may have some negative implications to specific northern communities – in particular, Fort McMurray and Fort Chipewyan, and possibly High Level – that are served in part by scheduled passenger service from the City Centre Airport. Those impacts include the possible reduction in scheduled air passenger services and carrier competition and reduced travel comfort. The extent of these impacts will depend on the responses taken by the carriers serving the affected communities.

Summary of Impacts: The impacts of the January 2004 access policy on the City Centre Airport and the airport's associated business community are expected to be moderately negative, reducing current levels of airport revenue and economic activity in the order of 10%. The most significant impacts are likely to stem from the heightened uncertainty and reduced confidence among businesses regarding the airport's prospects and the potential effects on their business intentions and future investments at that location. The modified access policy is likely to have a marginally positive financial effect on the International Airport.

Removing Scheduled Passenger Service Access

A policy that removes all scheduled service in the future would not be inconsistent with the results of the 1995 airport consolidation referendum and is within the authority of Edmonton Airports under its management lease with the City.

The implications of that potential access change are explored below. These implications are calculated independently of those resulting from January 2004 policy changes and are not in addition to them.

City Centre Airport Traffic and Revenues: Combined with the effects of the access policy changes planned for January 1, 2004, the potential loss of all scheduled passenger service at the City Centre Airport would have the effect of reducing the airport's current aircraft movements by 20% and the number of enplaned and deplaned passengers by more than 70%. The City Centre Airport's airside revenues would decline by an estimated \$1.2 million annually and the airport's land and hangar rental income would be affected through the loss of some aviation-related support businesses. The City Centre Airport's total revenues could be expected to decline by more than 40%.

The net impacts on the airport's financial performance would depend on management actions relating to operating and capital expenditures, fees and charges, and marketing and business development, and might be alleviated in some part by the growth in corporate and charter air traffic. As a result, Edmonton Airports challenges the OCA's conclusion that revenues would decrease by 40%, anticipating the impact to be closer to 25%.

Airport Business Community: The loss of aviation traffic at the City Centre Airport that would result from a discontinuance of scheduled passenger service would affect many establishments at the airport – some, very directly, through the loss of business associated with the reduced scheduled air traffic (e.g., fuel suppliers) and some more indirectly through spin-off effects related to lower business activity at the airport and reduced access and convenience for employees, customers, and suppliers. The overall revenues of airport businesses other than the scheduled carriers might decline by 10%. It would be expected that a number of businesses would choose to relocate or to discontinue operations and the financial capacity of some of those that remained would be impacted. The loss of businesses might also reduce the agglomeration synergies and the level of mutual reinforcement that now exist within the City Centre Airport business community.

A decision to curtail scheduled services would likely raise concerns by airport businesses that fees and rental charges might need to be dramatically increased to offset the loss of airport revenues. That concern as well as the reduced prospects and optimism for growth at the airport would have a very negative impact on continuing private aviation-related investment at the City Centre Airport.

For the predominantly business-oriented travellers that now use scheduled air services at the City Centre Airport, the loss of such services would imply extra travel time, inconvenience, and potentially extra cost. The magnitude of these impacts might be moderated to the extent that new corporate and charter operations are established at the City Centre Airport to serve the former scheduled air passengers.

International Airport: The curtailment of scheduled passenger service at the City Centre Airport would have the likely effect of redirecting some air traffic to the International Airport, particularly in respect of passenger services to and from Lethbridge and those northern communities now served by City Centre Airport carriers, as well as to shift some travelers toward the use of corporate or charter aircraft. The travel distances involved would make the affected destinations relatively unattractive to alternative travel by road in private vehicles.

With regard to short-haul traffic to and from Calgary, a sizeable share of the scheduled passengers now using the City Centre Airport is deemed likely to shift to travel by private vehicle and, to some degree, to corporate or charter aircraft. The remaining traffic could be expected to accrue to scheduled services at the International Airport.

Northern Communities: The City Centre Airport does not provide scheduled air passenger services to northern communities outside of Alberta. For the communities it does serve, alternative air service is available through the International Airport. However, the loss of scheduled services at the City Centre Airport would have varying degrees of impact on Fort McMurray, Fort Chipewyan, High Level, Grande Prairie, and Peace River, which could experience some reduced air service choice and competition. Many business travellers from the north prefer the access and convenience that the City

Centre Airport offers for conducting business in the city's downtown and a shift to the International Airport would infer some loss of convenience, extra travel time and, potentially, cost.

Summary of Impacts: The potential relocation from the City Centre Airport of all scheduled passenger operations would have a significant impact on traffic, revenues, and aviation activity at the airport. Airport revenues would decline by roughly one-half, and many establishments operating at the airport would be affected – to varying degrees – in operational or financial terms. The loss of scheduled services would significantly affect aviation prospects and aviation-related investment expectations at the City Centre Airport.

The International Airport would benefit from the relocation of some scheduled services and aviation businesses from the City Centre Airport. However, a share of the redistributed Calgary traffic would likely accrue to other travel modes, especially private vehicles, and some of the businesses that likely would move from the City Centre Airport would locate elsewhere in the region and to other centres in western Canada.