APPENDIX 5.1
(referred to in paragraph 5.117)

BA note on the prorate issue

Guide to airline prorating

1. Airlines often set through fares for journeys which involve more than a single flight, rather than charge the separate fares which would apply for the individual flights. Thus, for example, Air Canada offers[1] a fully flexible fare of $2,256 for travel from Thunder Bay to Frankfurt which allows transfer between flights at, among other places, Toronto. The equivalent fares for Thunder Bay–Toronto and Toronto–Frankfurt are $584 and $2,099, respectively, adding to $2,683. Thus the through fare provides a saving of $427 or 16 per cent over the fares for the separate legs.

2. In the example above all the travel is on a single airline, so that apportionment of the through fare is of no consequence but the same practice—through fares at less than the sum of the fares for the separate legs—applies with respect to many journeys which involve more than one airline. For example, BA offers the same fares as Air Canada for each of Toronto and Thunder Bay to Frankfurt even though it can carry passengers only between Toronto and Frankfurt[2] and therefore needs to use another airline for the Thunder Bay–Toronto leg.[3] This inevitably raises the issue of how the through fare should be apportioned between the two airlines involved. Within the industry an agreement, to which most airlines adhere, has been reached on how this should be done (the Multilateral Prorate Agreement or MPA).

3. The basic method of allocating a fare between participating airlines is known as straight-rate prorating (SRP). Under SRP the fare is divided up between the airlines in proportion to their shares of the 'prorate mileage' of the journey.[4] However, the system allows an airline to file a 'proviso' in respect of any part of the journey which is on its services, provided that sector is not more than 3,000 prorate miles. Provisos are usually specified as proportions of the sector fare. For example, an airline may specify that it requires to receive the same amount as it charges passengers for its part of the journey on a stand-alone basis or it may say that it requires 90 per cent, 80 per cent or some other percentage of that fare; sometimes it will specify different percentages for different types of fares (for example, 90 per cent for unrestricted fares or 60 per cent for low promotional fares). Different provisos may also be specified for different types of journey (for example, 80 per cent for a sector which is part of a journey wholly within North America and 100 per cent for the same sector when it forms part of any other journey). When there are provisos filed for sectors of a journey, they are taken out of the fare and the balance is prorated using SRP over the balance of the journey. In some cases the effect of these provisos could be to leave one participating airline with next to nothing for its sector; indeed the provisos could add up to more than the fare.[5] There is, therefore, a protection built into the system, which is such that if any airline would receive less than a specified amount[6] then all provisos are ignored and proration is completed using SRP.

4. Clearly, for this system to work there is a need to know the prorate mileage and airlines' basic fares[7] for each sector that may appear in a journey. This information is gathered by an agency, 'The Prorate Agency', and published to all the airlines quarterly, along with airlines' prorate provisos.

5. For North American airlines the basic fares are captured from the airlines' fares filings submitted to ATPCo, the agency used by all such airlines to file fares with regulators, where necessary, and with

[1]The fares quoted were as shown in CRSs on 4 May 2000 for travel on 1 June 2000.
[2]The journey would involve a connection between BA services at London.
[3]Prior to the Air Canada takeover of Canadian Airlines, BA would have used Canadian Airlines but now must use the combined entity.
[4]The prorate mileage for the journey is the sum of the prorate mileages for each leg. The prorate mileage for a leg is the product of the great circle distance between the end points of the flight multiplied by a factor to take account of relative differences in unit costs between short and long and between flights of similar length in different parts of the world.
[5]Air Canada would sell a fully flexible economy ticket from Toronto to Cairo for $2,533 which permitted the passenger to fly via any number of intermediate stops. If the passengers chose to stop at London and then fly to Brussels with Sabena, on to Zurich with Swissair, to Athens with Olympic and finally to Cairo with Egyptian and each of those airlines applied a prorate proviso requiring its full sector fare, then Air Canada would be required to pay them $473, $576, $1,144, and $470, respectively, a grand total of $2,663 or $130 more than Air Canada had collected for the entire journey.
[6]The specified amount is calculated in effect by multiplying the prorate mileage for the sector concerned by a rate per mile, specified in US cents and adjusted annually in accordance with a fixed formula. The amount is currently 8.8 cents.
[7]A basic fare is determined for each cabin class (eg First, Business and Economy) which an airline offers on the sector.

the CRSs used by travel agents and others for obtaining information about available flights and fares and for making bookings.[1] For all other airlines, the data are captured from manual filings made with the prorate agency in accordance with specified rules.[2]

6. In addition to the MPA, many airlines have bilateral agreements with other airlines covering the way that revenues on all or particular journeys involving the two of them shall be divided. Alliances sometimes extend these agreements to multilateral ones involving several or all the members.

Prorating and Air Canada

7. BA and others have expressed concern about the possibility that Air Canada might use its near-monopoly of Canadian domestic scheduled transport, following its acquisition of Canadian Airlines, to adjust its prorate requirements so as to have the effect of rendering uneconomic competition with it for international traffic to and from points behind international gateways. This section explains these concerns and why Air Canada's recent behaviour gives them added strength.

8. Air Canada is party to the MPA. In the latest quarterly publication of prorate provisos (March to May 2000) applicable to that agreement, Air Canada publishes many provisos. BA's main concern is in respect of the prorates for Canadian domestic sectors forming part of a journey between Canada and the UK. The provisos published in the latest manual for such sectors are as follows:

(a) for First and Business class normal fares[3]—100 per cent of the base amount;[4]

(b) for Economy normal fares—100 per cent of the base amount;

(c) for Excursion[5] fares originating in Canada—100 per cent of the base amount;

(d) for Excursion fares originating in the UK—70 per cent of the base amount;

(e) for Super Apex[6] fares originating in the UK—70 per cent of the base amount except in respect of travel between seven pairs of points within Canada when the amount varies between 34 per cent (Ottawa–Toronto or vv) and 100 per cent (Toronto–London Ontario or vv);

(f) for Super Apex fares originating in Canada—100 per cent of the base amount;

(g) for Apex fares originating in the UK—70 per cent of the base amount except for travel between 11 pairs of points within Canada when the amount varies between 31 per cent (Toronto–Calgary or Edmonton or vv) and 100 per cent (Toronto–London Ontario or vv and Vancouver–Nanaimo or Victoria or vv);

(h) for Apex fares originating in Canada—100 per cent of the base amount;

(i) for Pex[7] fares originating in the UK—70 per cent of the base amount except in respect of travel between nine pairs of points within Canada when the amount varies between 34 per cent (Ottawa–Toronto or vv) and 100 per cent (Toronto–London Ontario or vv);

(j) for Pex fares originating in Canada—70 per cent of the base amount; and

(k) for other fares—70 per cent of the base amount.

---

[1]The basic fare captured for North American airlines is the highest unrestricted fare for the particular class available for sale for the sector at the date of capture.

[2]The rules require that the fare is available for sale for travel on the sector on a specified date (the first day of the quarter concerned). Although airlines may file as their basic fare any fare meeting this condition, in practice they usually file the highest such fare, replicating what happens in respect of the North American airlines.

[3]Normal fares are the fully flexible fares.

[4]The base amounts are the basic fares, the highest fare level available for sale, on the sector and in the class concerned, at the date of capture of data for the quarterly manual.

[5]Excursion fares are relatively unrestricted fares designed typically for personal travel.

[6]Apex fares are fares with a requirement that they be purchased more than some specified time before travel. Super Apex fares have longer purchase lead times than Apex fares and will usually be cheaper than Apex fares.

[7]Pex fares are quite restricted fares but without any requirement that they be purchased by any particular time, that is, they can be bought any time up to the time of travel. They will generally be cheaper than Excursion fares but dearer than Apex fares.

9. In practice, in many cases these provisos will not apply because they would lead to the transatlantic leg's recovering less than the minimum permitted; therefore straight rate prorating will apply. For example, the prorate mileage for Toronto–London (UK) is 4,299 miles and the minimum rate that an airline must receive for that sector after any proviso has been applied is US$0.088 per mile[1] or US$378.31, which is about CA$560. This means that for a round trip the transatlantic airline would have to receive at least CA$1,120. Air Canada's promotional fares (ie everything except the normal fares) for Ottawa–London in June 2000 range from CA$799 to CA$1,337, return. Assuming that another airline competed with it at these fare levels but routing its passengers over Toronto, then it is clear that only at the very highest end of this range would there be any prospect of Air Canada's being able to obtain a proviso on the domestic sector without taking the transatlantic airline's take down below the minimum.

10. Where the provisos will tend to bite is in respect of the normal fares, particularly in business and first class. Using the same journey as an example, Air Canada's normal fares in economy, business and first class from Ottawa to London are CA$1,357, CA$2,250 and CA$4,698, respectively, one way. This means that any prorate proviso for the Ottawa–Toronto leg which is not more than $797, $1,690 or $4,138 in each class, respectively, would still leave the transatlantic airline with more than the minimum and would therefore be applied. These compare with Air Canada's current highest fares on the Ottawa–Toronto route of $333 and $389 in economy and business classes, respectively. If, in accordance with Air Canada's proviso, it is paid 100 per cent of the local fare for the Ottawa–Toronto leg, a competitor which competes with it in the Ottawa–London market by matching its fares over Toronto would be left with CA$1,034, CA$1,861 and CA$4,309 for economy, business and first classes respectively for the Toronto–London leg. These compare with Air Canada's own prices for Toronto–London as a separate journey of CA$1,357, CA$2,250 and CA$4,781 in economy, business and first respectively.

11. It will be seen that, since Air Canada's fares from Ottawa to London are the same as or lower than its fares between Toronto and London, any competitor trying to compete with its direct services Ottawa–London is already at a disadvantage, in that whatever the prorate it has to pay Air Canada for the Ottawa–Toronto leg, it will end up with a discount on the point-to-point fare for Toronto–London. The proviso Air Canada publishes, applied using its current published fares for the domestic sector, makes this discount substantial. But the action Air Canada took earlier this year made the discount prohibitive and would provide it with a prorate for its sector much greater than its own highest fare for the journey.

12. In the last week of March, Air Canada made changes to its domestic fares. It redesignated its existing highest, fully flexible fares in each class. Prior to the redesignation, the fares were labelled 'J' and 'Y' in business and economy, respectively. In the new structure the same fares, with identical conditions, were redesignated 'J1' and 'Y1', respectively, and new much higher fares, indistinguishable in conditions, were added using the old designations J and Y. These fares were available for sale and travel for about three weeks. This covered the period in which the Prorate Agency collected data for its quarterly publication. It, in accordance with its rules, would have selected these higher fares as the base amounts for the next quarter (June to August) in place of the previous amounts, now represented by the new J1 and Y1 fares. Of course these higher fares would not actually be bought by passengers, since they provided nothing that the much lower J1 and Y1 fares did not provide.

13. The effect of these changes on Ottawa–Toronto–London is to raise Air Canada's prorate proviso from CA$389 for business class normal-fare passengers to CA$1,143. This will leave the transatlantic airline which is matching Air Canada's fares for Ottawa–London with CA$1,007, or 45 per cent of the fare for Toronto–London on its own, while Air Canada gets 14 per cent more, amounting to nearly three times its highest fare for the Ottawa–Toronto leg.

Source: BA.

[1]This is the present rate but it varies from year to year.