

AIRLINE - TRAVEL AGENT RELATIONS:
AN EVALUATION OF REMUNERATION SCHEMES

by

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Abstract

Travel agents provide an essential range of air travel marketing services which result in large commission expenses for air carriers. Commission expenses have risen to such an extent that air transport analysts and others in Canada have openly criticized remuneration policies now in practice. They have questioned whether the travelling public is receiving a full value for the commissions which travel agents receive; they have cited rising commission expenses as evidence of economic inefficiency within the air travel marketing system.

The role which the travel agent plays in the airline industry is described taking into consideration travel agents, air carriers and air passengers. Relevant background information related to the travel agent remuneration issue is presented by describing issues affecting the ability of independent agencies to provide travel services.

This thesis approaches the travel agent remuneration problem using policy analysis to select a remuneration scheme which will best satisfy a select list of objectives. The objectives used in the evaluation of remuneration schemes include service objectives such as retaining travel agent impartiality, economic objectives such as implementing the "user pay" philosophy, political objectives such as avoiding obvious cross subsidization of different user groups and "regional development" objectives such as providing adequate service levels to small communities.

Description of developments in issue areas including travel agent industry entry requirements, competition for market

segments and the introduction of electronic reservations systems to travel agents is presented in order to better understand the likelihood of remuneration schemes achieving objectives.

Three basic types of remuneration alternatives, net fare, uniform commission and incentive commission are considered.⁸³ Both regulated and unregulated incentive commissions are analyzed since their impacts vary significantly. The regulated incentive commission alternative is selected as the optimal travel agent remuneration scheme. The selection of this alternative results in a compromise between the full achievement of the various objectives. Under this alternative, the benefits and costs of regulatory involvement in the setting of remuneration levels are assured.

⁸³The net fare remuneration alternative may be defined as a marketing scheme where travel agents receive no commission on ticket sales instead, a service fee is charged. Under a uniform commission payment scheme, all travel agents receive the same percentage commission payment. Incentive commissions offer travel agents financial incentives for high volume sales or for sales to particular destinations.

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CHAPTER 1 INTRODUCTION

1.0 Introduction

There is little doubt that travel agents play an essential role in the airline industry by providing services to air travellers. The airline industry has relied upon the services offered by the travel agent industry because of the numerous advantages which an independent channel of distribution has in comparison with airline-owned channels of distribution.

The traveller contemplating flying from New York City to Chicago is faced with choosing from among 6 different carriers and 75 direct flights as well as numerous connecting flights.¹ Individual carrier's city ticket offices tend to a large extent to emphasize the sale of their own air transportation product while deemphasizing the sale of competing carriers. The result for the passenger may be a longer travel time than is necessary because a carrier with an indirect routing is selected. Therefore, a lower level of customer service results. In this situation, the unbiased consulting services provided by the travel agent can eliminate delays and provide air travel services in a more convenient manner.

¹Official Airline Guide-North American Edition, Oak Brook, Illinois, Reuben H. Donnelley, November 15, 1977, p. 274.

Travel agent services are particularly important in the international sector where travellers are generally less familiar with the variety of transportation, accommodation and other travel services offered. Consider, for example, the case of the family travelling abroad on a limited budget. The individual travel agent is much more likely to present low-cost alternatives to the traveller than would an airline selling its own services. Similarly, the travel agent will most likely be familiar with alternate modes of transport providing a different range of services but frequently deemphasized in airline sales offices.

Throughout the analysis of problems confronting the travel agent industry presented in this thesis, one should bear in mind that travel agents, in the context of the airline industry are by definition appointed sales representatives which serve as channels of distribution; they do not produce transportation services per se, but rather, serve as sales intermediaries, receiving a commission for the services which they provide their clients.

1.1 Thesis Objective

As a general frame of reference, a multi-faceted approach bringing into consideration consumers, travel agents, air carriers and government regulatory agencies is taken in examining the changing role of the travel agent in the air transportation industry. More specifically, the objective of the pages which follow is to select a travel agent remuneration policy for Canadian travel agents which is in the long-run best

interest of the travelling public. A subsidiary objective is to evaluate the need for regulation of the travel agent industry in order to retain desirable attributes associated with the travel agent industry.

In order to achieve this, present airline-travel agent remuneration policies are described; alternatives are generated; and analysis of the costs and benefits and the impact of each alternative is studied. Finally, an alternative is selected and presented as a suggested policy change for implementation by the Canadian Transport Commission.

1.2 Limitations And Assumptions

There are primarily two major limitations to the degree of comprehensiveness of this thesis. First, the analysis of problems limits itself to considering the usefulness of travel agents in the airline industry. Although the non-air modes play a significant role in the travel agent industry, a recent study revealed that 37 percent of the total dollar volume of travel agent sales was derived from non-air mode sales.² Second, the focus of attention of the analysis presented is upon retail as opposed to wholesale travel agents. The involvement of airlines in tour wholesaling through the ownership or control of wholesale travel agencies is dealt with in a tangential fashion.

It is assumed that the impact of rising commission levels in Canada shall be similar to the changes which have resulted in

² Louis Harris and Associates, The Character and Volume of the United States Travel Agency Market, New York, N.Y., Ziff-Davis Publications, April 1977, p. 10.

the United States. However, due to differences in characteristics of both the travel agent and airline industries, primarily related to size differences, this is not necessarily true in all respects. One should bear this in mind that this thesis considers policy alternatives in a Canadian setting.

1.3 Benefits And Costs From Travel Agent Services

Benefits And Costs For The Consumers

As of 1977, there were more than 2,000 tour operators and travel agents providing convenient locations to clients in most Canadian communities.³ Convenience in location and the associated one step shopping are two attractive features which travel agencies as small businesses offer the travelling public.

Uniform commission structures have been developed in order to ensure the unbiasedness of the travel agent in the selection of carriers. For example, under the 1977-78 commission structure prevailing in Canada, a 7.5 per cent commission paid on domestic ticket sales by both Air Canada and CP Air, it was in the best interest of the agent to select the flight which is most convenient for the customer.

As small business concerns, travel agencies are in a better position than airline owned city ticket offices to provide clients with personalized travel consulting services which

³The number of travel firms in Canada during 1977 is drawn from "The Big Business of Travel," The Financial Post, March 26, 1977, p.T-1.

extend much further than merely booking a seat on a flight or making a hotel reservation. Consumers of air travel services benefit from the specialization of travel agents into various market segments such as the commercial travel or the ethnic market segments.

Of course, the service benefits obtained by consumers from travel agents are not obtained without incurring a cost. However, providing a precise answer to the question, "Who pays for the services performed by the travel agent?" is not easy to do. The impact of travel agent costs depends upon the bargaining power of the participants in the airfare commission determination process. If carrier conferences succeed in passing the cost of high commission rates along to users in the form of higher airfares, then it is clear that the services offered by travel agents are not, in fact "free" from the consumer's point of view. On the other hand, if commission levels rise but a strong regulatory body is able to restrict increases in airfares, then, ceteris paribus, airlines will for the most part earn lower profits. Similarly, assuming that the cost of providing services would be greater without the travel agent, there is no real cost associated with the use of travel agents.

Benefits and Costs for the Airlines

Another key benefactor from the services performed by travel agents is the air carrier. The rationale underlying the reliance upon travel agencies is essentially founded upon the belief that it costs the carrier less to market its product through an appointed agent than what it would through city sales

offices. Clearly, it would be economically inefficient for each carrier to establish as many ticket outlets as there are retail travel agencies. Even if each airline established only a modest fraction of the over 14,000 agencies presently approved by United States carriers, marketing costs would be much greater than commissions which are presently paid.⁴

The fact that airline managers are highly concerned with minimizing travel agent commission expenses while at the same time providing adequate customer service levels should also be kept in mind when analyzing the remuneration alternatives presented in this thesis.

Benefits and Costs for the Owners of Travel Agencies

The most obvious beneficiaries from the services offered by travel agents are the shareholders and proprietors of individual business enterprises.

Recent Air Traffic Conference statistics reveal that in the United States, sales per location rose at a compound rate of approximately 8% during the period from 1969 to 1974, a period when the number of travel agency locations was increasing.⁵ Evidence of the increase in travel agent sales per location is revealed in Exhibit 1. It should be kept in mind when evaluating this data that travel agencies are generally composed of a number of sales outlets, hence total firm earnings would be

⁴"Travel Agent Commissions Reach \$1.44 Billion in 1976," Air Transport World, October 1977, p.32.

⁵Air Traffic Conference of America, "Travel Agent Commission Structure," Washington D.C., 1974, p.3.

greater than sales per outlet.

Exhibit 1.

United States Travel Agent Sales Per Location

<u>Year</u>	<u>Thousands Of Dollars</u>	<u>Index</u>
1969	299	100.0
1970	318	106.4
1971	330	110.4
1972	358	119.7
1973	368	123.1
1974	432	144.4

Source: Air Traffic Conference Of America, "Travel Agent Commission Structure", Washington D.C., 1974,

p.3.

Recent data drawn from a Canadian setting indicates that the average agency produces \$900,000 to \$1 million in sales annually with net earnings varying widely from 0 to about 4 percent of gross revenues, the average being around 1 percent.⁶

Fringe benefits such as instructional tours and reduced transportation fares attract many individuals to the travel agent industry, an industry which has generally been characterized as having long working hours and relatively low pay. The fringe benefits which travel agents receive are frequently untaxed (and thus all-the-more attractive), reflect a relatively low cost to the airline industry in comparison with

commission expenses.

1.4 Outline Of Remaining Chapters

Chapter 2 describes existing commission remuneration procedures, generates alternative compensation schemes and presents the advantages and disadvantages to interested parties of the various alternatives. The three chapters immediately following Chapter 2 are concerned with separate problems facing the travel agent industry resulting from environmental changes. Chapter 3 reviews the history of travel agent legislation and evaluates its impact upon carriers, travel agents and the public. Chapter 4 considers unique services offered by travel agents to particular segments of the travel industry such as the ethnic and commercial travel markets. The following chapter, Chapter 5, considers the impact of technological changes upon the retail travel agent industry. In particular, the advantages and disadvantages for consumers, carriers and travel agents of the introduction of electronic reservations terminals to the industry is dealt with. In Chapter 6, the impacts of the various remuneration alternatives upon travel agents, carriers and the travelling public are evaluated and one remuneration scheme is selected as the most desirable given a select set of objectives. The method of selecting these objectives plays an integral role in analysis of the commission issue presented in this chapter.

⁶"Licensed Leisure", The Financial Post, Supplement on the Canadian travel industry, March 26, 1977, p. T-2.

CHAPTER 2 TRAVEL AGENT REMUNERATION APPROACHES

2.0 Domestic Commissions

In the United States, the federal agency which regulates the commissions which travel agents receive on ticket sales is the Civil Aeronautics Board (C.A.B.). This regulatory body requires that all commission structures for sales of air travel services originating in the United States be filed with the Board. Under this system, carriers are free to pay travel agents whatever commission they feel will maximize profits provided that it is filed with the government agency.

In Canada, the regulatory situation concerning commissions is somewhat different. The Canadian Transport Commission's Air Committee is not required to approve commission structures even though it reserves the right to disapprove of commission structure changes which may, in its view, be detrimental to the survival of the airline industry. An example of the exerting of the regulatory power of this body occurred in 1977 when Pan American World Airways attempted to introduce incentive commissions to Canadian agents but was prohibited from doing so.⁷

The result of this situation has been that the two major

⁷ "Pan Am Cannot Offer Incentives to Agents Here", Canadian Travel Courier, October 7, 1976, p. 1.

Canadian carriers, Air Canada and CP Air, as well as the regional carriers have followed the commission structure established for U.S. carriers with respect to domestic and transborder travel; the latter of which is generally defined as travel between Canada and the United States. Aside from reasons of competition, the major reason for this is the requirement of the Air Traffic Conference of America (ATC), that member airlines follow the same commission structure. One should note at this point that Air Canada and CP Air are associate members of the ATC.

As of April, 1978, domestic commission structures were the same for both Air Canada and CP Air. This commission structure which is shown in Exhibit 2 provides agents with a monetary incentive to sell transportation services incorporating services in addition to air transportation from point A to point B.

One must differentiate between the various tours which pay different commissions. The ATC defines four different tours: advertised air tours, convention air tours, independent air tours and incentive air tours.⁸ As of April, 1978, advertised and independent air tours offered travel agents an 11 percent commission whereas incentive and convention tours offered only a 10 percent commission.

Advertised and convention air tours are package tours and must include air transportation as well as one additional travel related component such as ground transportation, hotel

⁸Air Traffic Conference of America, Trade Practice Manual, Resolution No. 80.15, December 31, 1975, p. 19.

accommodation or a sightseeing tour. Independent air tours are prepaid tours including travel to two non-contiguous North-American cities or localities. The agent must advertise and make promotional efforts in order to qualify for the independent tour commission. Incentive tours are comprised of circle trips as well as other accommodations and tourist related activities. In order to qualify for incentive commission rates, such tours must be promoted with printed promotional literature.

The rationale underlying differential commissions for the various tours stems from the belief of the conference that agents should receive greater compensation for sales which are more expensive to service.

Due to the economic incentive for travel agents to seek to increase the ratio of revenues retained over total sales revenues, the tendency to claim that ticket sales qualify for higher tour commissions was reported to have increased rapidly⁹ especially before the widespread use of differential commissions in the international market. This could be expected as the revenue altering variables which retail travel agents may alter are rather limited. Moreover, from the individual firm's point of view, there is a substantial difference between the previous commission level of 7 percent and one of 10 or 11 percent.

Commission levels for domestic air transportation in Canada and the United States have remained relatively non-competitive over the last decade because of the strength of the ATC and

⁹Interview with Phillip Morgan, CP Air IATA representative, March 15, 1977.

because the appropriate regulatory bodies have not rejected commission rates filed with them. Some concern has been expressed by the domestic carriers that the commission rate phenomenon which has developed for international commissions will spread to include domestic commissions as well, thereby precipitating increased marketing costs to the domestic airlines. The similarities between an open rate situation for domestic commissions and an open rate situation for international commissions are significant. Indeed, if the open rate were allowed to spread, the profitability of domestic carriers would most likely be reduced given the high variability of commission expenses as a percent of the total operating expenses.¹⁰ The costs and benefits of the open rate commission situation as well as a view as to whether regulatory control of commissions is in the public's interest shall be presented in the latter part of this chapter.

2.1 Commissions On International Air Transportation

Conference Ticket-Clearing-Procedures

The International Air Transport Association (IATA) has designed a set of procedures which it calls the Agency Programme in order to ensure that all agency outlets are "competent and

¹⁰Evidence of the relative importance of increasing commissions to the ATC member carriers is revealed in 1977 Air Transport Association of America statistics. Over the period from 1975 to 1976 passenger traffic commissions representing 4.9% of operating expenses increased by 17.7 percent while labour costs increased by only 10.4 percent. Aviation-Daily, January 10, 1977, p.63.

ethical organizations capable of providing accurate and dependable service to the public".¹¹

Exhibit 2

CP Air Domestic Schedule Of Commissions For Air Transportation Originating In The United States

Commission On Domestic Canadian And Transborder Transportation

Charter Class Hawaii Fares	10 %
Charter Class Canada Fares	8 %
Family Plan Fares	8 %
7/30 Day Excursion Fares	8 %
30 Day Excursion Fares	8 %
Discover America Excursion Fares	8 %
Extraterritorial Trips	7 %
Group Fare Travel	7 %
Discount 20-Air Travel North America	7 %
All Other Domestic/ Transborder Fares	7 %
Charters	5 %
Advertised/Independent Air Tours	11 %
Incentive/Convention Air Tours	10 %

Source: CP Air, Marketing Department, April 1978.

The specific requirements of IATA concerning agency entry

¹¹J. Brancker, IATA and What It Does, Leyden, The Netherlands, 1977, p. 60.

requirements shall be examined in Chapter 3 which is concerned with industry regulation.

One of the primary reasons for the founding of the Agency Programme was to prevent agencies from discounting from established ticket price by splitting their commissions with customers. The carriers felt that in the long-run, it would be in the interest of the public to establish regulations which forbid member carriers from paying commissions to non-IATA approved travel agencies. Efforts on the part of IATA to foster an industry characterized as financially stable and professional in character have been thwarted to a certain extent by agents who lend their ticket stock to non-IATA approved agencies.

The IATA Bank Settlement Plan

A payment settlement plan created by IATA establishes a central clearing house for payments of IATA approved travel agents to member carriers. These clearing houses (which are typically commercial banks) allocate the receipts to the appropriate airlines. The utilization of financial intermediaries is more efficient than a system which would call for each carrier to remit payments to each of a number of carriers.

The advantages of this system which accrue to the travel agent include simplified reporting and remitting procedures and the centralized issuance and control of all sales documentation and the automatic replenishment of ticket stocks. Similarly, the air carriers benefit from the lower cost of the system as compared with what would be the case under a system which

collected from each travel agent separately. Annual ticket sales handled by the system reached \$1.1 billion in 1977.¹²

The International Travel Agent Remuneration Conflict

Traditionally, IATA has played an instrumental role in the establishment of agreed upon commission structures for international air transportation. International commissions have generally been somewhat higher than those paid on domestic ticket sales.¹³ The primary reason for this stems from the conference belief that travel agents devote more time and effort in assisting and planning an individual's journey abroad than is required for a shorter domestic journey, which is an allegedly less complicated matter. Although this reasoning was quite valid in the earlier days in international air transportation when only the affluent could afford the luxury of international air travel, one wonders whether the difference between international and domestic commissions, at least before 1975, was not a vestige from the past.

With the rise of the excursion fare and the emergence of charter flights, especially on the North Atlantic, and the increased frequency of travel in that market and more importantly the increased access to international air travel to a wide cross section of the public, the argument for a difference between international and domestic commissions no

¹²Ibid., p. 63.

¹³Agents do not receive international commission rates for sales on transborder flights between Canada and the U.S. Such sales receive remuneration at a special transborder commission level.

longer is very convincing. There appears to be no indication that the industry shall adopt a blanket or uniform commission level. Indeed, the opposite appears to be the trend taking hold.

The international commission structure prevailing up until April of 1975 offered travel agents in Canada and the United States 7 percent on international point-to-point ticket sales and 10 percent on the sale of inclusive tours. However, this situation could not endure forever. Following the phenomenal growth patterns of the airline industry in the 1960's and the introduction of numerous technological advancements to the industry, most carriers were prepared for continued strides forward in the 1970's. Industry economists and management faced grave difficulties in meeting the demands on their organizations inflicted by environmental changes such as spiraling inflation, the "energy crisis" and a leveling off of demand for air travel in many markets. One should also recall that these changes came about at a time when most carriers had expanded capacity by entering the wide-body era in anticipation of future traffic growth. The upshot of this situation was that individual carriers became tempted to alter commissions, one of the marketing mix variables not directly regulated by government agencies. The practice of rebating passenger fares to agents and offering commissions higher than those agreed upon by conference regulations became widespread in the early 1970's due to the short-term benefit of increased traffic.

The wide variety of compensation schemes and overrides offered by carriers to agents were not required to be filed with the Civil Aeronautics Board at that time. Thus, from a competitive

point of view, it became exceedingly difficult for the individual international carrier to keep track of the commissions offered by each competitor on each route. The situation progressed in such a manner until Pan American World Airways announced in April of 1975 that it would no longer abide by IATA rules concerning commissions because other carriers were offering illegal discounts, rebates and kickbacks. Instead of following the clandestine course which much of the industry had taken, Pan American developed the volume incentive commission plan and began openly paying a 3 percent override for all sales in excess of 90 percent of the business each agent supplied Pan American in the comparable month of the previous year.¹⁴

The rationale underlying the denunciation of the IATA commissions is found in excerpts from a letter by William T. Seawell, Chairman of the Board of Pan American to the Director General of IATA. Pan Am's actions touched off an open rate commission situation which has had significant ramifications for airline-travel agent relations. The course of action Pan Am chose to take as well as the reasons underlying the major international carrier's decision are evident in the following communique:¹⁵

¹⁴"Agent Commissions Stir Concern", Aviation Week and Space Technology, April 14, 1975, p. 25.

It is common knowledge that IATA commission resolution are being widely ignored. Business controlled by agents has become, to a significant extent, the subject of competitive bidding of various airlines. The problem has become most serious in recent weeks as traffic levels have declined and as carriers have sought to fill empty seat capacity. Violators have found comfort in the fact that IATA does not or cannot enforce its resolutions...

The present violations discriminate against those airlines and agents who have sought to observe resolution. The impact on Pan Am has become most serious... We can no longer explain to our stockholders, creditors, and employees why Pan Am's position should be eroded through adherence to standards that others successfully ignore.

Given the fact that Pan Am cannot afford to observe resolutions that no longer exist in practice, Pan Am must choose between joining secretly others in violating these resolution or of meeting the situation publicly and honestly. We are convinced that it is best for the travelling public, and travel industry and IATA to bring this matter into the open and to deal with it directly.

We have concluded that the soundest and least disruptive course of action lies in denouncing the agency resolutions... The commission resolutions are being breached consistently and extensively by an increasing number of subscribing carriers who are unfairly profiting from Pan Am's good faith adherence. IATA, which is charged with enforcement, is unable or unwilling to carry out its assignment. Given these facts, there is no reason why Pan Am should continue to regard itself as bound.

Management at Pan American succeeded in achieving the objective of drawing attention to the badly needed reform of the

¹⁵United States, Civil Aeronautics Board, "IATA Agreements Concerning Agency Matters--Uniform Commission Rates", Docket No. 28672, March 15, 1978. pp. 3-4.

IATA commission resolution. Moreover, they were successful in exposing the weakness of the conference's compliance procedures which are supposed to be designed to eliminate carrier and travel agency violations of IATA resolutions. The actions of one carrier could not, of course, go unnoticed. Other carriers including CP Air, British Airways and Trans World Airlines followed suit and gave notice of rescission of agency commission resolutions; shortly thereafter, they announced new variations to their own commission structures.

Carriers reacted in a variety of ways. British Airways was reported to have offered U.S. agents a straight cash bonus for any ticket sold incorporating its route network. Iberia, the Spanish national carrier, increased its commissions to 10 percent on all sales.¹⁶ Trans World Airlines announced an 8.5 percent commission on certain routes.

IATA responded to the Pan Am proposal by augmenting the overall level for international point-to-point sales from 7 percent to 7.5 percent. One must bear in mind the estimate by travel agency organizations that a 1 percent increase in commissions would cost airlines approximately \$165 million annually on a world wide basis.¹⁷

Rulings of the U. S. Civil Aeronautics Board concerning

¹⁶R. K. Elingsworth, "Pan Am Inflexible on Agent Fee Reform", Aviation Week and Space Technology, June 23, 1975, p. 23.

¹⁷A survey of 27 carriers representing 51 percent of world airline passenger traffic revealed that agents generated some 55% of all passenger revenues. Assuming world airline revenues of \$30 billion, a 1 % increase in commissions would cost world airlines approximately \$165 million annually. Op. Cit., Air Transport World October, 1977, p. 32.

commission levels have had a significant impact upon the airline industry and in particular upon the relationship between travel agents and air carriers. Subsequent to Pan American's notice of rescission of IATA commission resolutions, the C.A.B. issued a notice requiring all carriers, both American and foreign, to maintain a filing for public disclosure, reports of all commissions and other compensations paid travel agents for services rendered. The agency also established regulations which forbid carriers from compensating travel agents and tour wholesalers at levels not on file with the Board. Although this move facilitated the efforts of carriers to keep track of competitive commission levels, it did not result in the Board's acceptance of a conference commission structure agreement.

2.2 Open Rate Commissions

An open rate situation has prevailed on commissions received by U.S. travel agents for international travel originating in the United States since the abandonment of IATA commission resolutions by Pan American.

Canadian carriers which serve international markets have, to some extent, been able to isolate themselves from the escalating commission levels in the United States. The threat of the diversion of traffic to U.S. carriers has been suppressed by the prohibition maintained by the Canadian Transport Commission regarding the payment of higher commissions to Canadian travel agents. For example, in October of 1976, Pan American was reported to have been prohibited from paying commissions above the 8 percent/11 percent level which Air Canada and C P Air

maintained as their international commission structure.¹⁸

Nevertheless, it is apparent from interviews with travel agents and reports in industry publications that agents have devised methods of circumventing C.T.C. regulations in this regard. One approach utilized in obtaining higher commissions is for the Canadian agency to make sales on the international ticket stock of an affiliate agency in the United States. Another approach which has recently developed, is the payment of illegal overrides in the form of additional tickets on carriers for which no payment is made to the issuing carrier. This form of override payment came to the attention of Revenue Canada inspectors who were concerned that agents were not reporting tickets as income.¹⁹ The above situations exemplify the significant extraterritorial impact of U.S. regulatory agency decisions upon the air transport industry in Canada.

The open commission rate situation has attracted a great deal of attention both within the travel industry and from the public as well. One might attribute this interest to the dramatic change in commission levels over the past five years, where prior to 1975 agents were earning 10 percent commissions on sales of group tickets on the North Atlantic as opposed to the 25 percent level of commissions which British Airways was reported to be paying in February of 1977. Exhibit 3 indicates the heterogeneity of commission rates prevailing for U.S. travel

¹⁸"Pan Am Incentives Prohibited", Canadian Travel Courier, October 7, 1976, p. 13.

¹⁹"Revenue Canada Investigate Illegal Rebates", Canadian Travel Courier, March 9, 1978, p. 1

agents selling international air transportation at the same time that the 25 percent British remuneration level was reported.

Exhibit 3	
Selected International Commission Levels-February 1977	
<u>Airline</u>	<u>Commission Level</u>
Aerolineas	Basic Rate 10 To 11 Percent
Argentinias	
Air New Zealand	Group Overrides To Selected Agents Of Between 10 And 15 Percent
Air Siam	30 % On Individual Tickets; 41 % On Group Sales
Alitalia	23 % For Milan Or Rome Bookings; 3 % Override For Tours
British Airways	Override Of Between 3 % And 17 % To Selected Agents
El Al	Incentive Payments To \$60 On Individual Payments
KLM	Overrides Of Between 2 % And 8 %
Pan American	23 % Commission On Certain Routes
TWA	Paying A Variety Of "developmental" Commissions
Source: R. K. Ellingsworth, "Agent Commissions Stir Concern", <u>Aviation Week And Space Technology</u> , February 14, 1977, P. 23.	

The open commission situation has aptly been termed a "commission war" by industry observers because of the dramatic increases in sales which are possible in markets with a high proportion of sales through travel agents.

The United States-Italy market is a case in point. At the beginning of 1977, Alitalia, the state-owned Italian flag carrier, introduced higher commissions on the North Atlantic.

The airline offered to pay agents an additional 15 percent over and above the standard 8 percent offered by most carriers.²⁰ Moreover, an additional incentive override of 3 percent was offered for itineraries including tours. For the travel agent deciding upon a carrier for a New York-Rome passenger, the \$348.22 commission offered by Alitalia on a \$1,514 round-trip first class ticket was more attractive than the \$148.69 commission offered by TWA. Although this is an extreme example, it does point out the effect upon the impartiality traditionally associated with the travel agent.

A summary of competitive carrier passenger commission filings with the U.S. Civil Aeronautics Board is presented in Appendix 1. From this data, one observes not only the wide diversity of group overrides and volume incentives, but also the type of performance and sales patterns which individual carriers are attempting to foster. Average commission levels have increased substantially since the introduction of open commission structures. Although conference regulations forbid the discounting of airline ticket prices by sales intermediaries, higher commissions on highly competitive routes have resulted in increased temptation for travel agents to indulge in illegal fare discounting in order to remain competitive. The passing on of lower ticket prices to end users is an economic phenomenon which one would expect under conditions typified as having a great deal of competition and

²⁰"Airline Commissions Go Sky High", Business Week, February 7, 1977, p.31

limited government or conference control.

In Japan, where the Japanese government eventually stepped in, the commission situation developed to a point where airlines were reported to be keeping as little as half of the published ticket price.²¹ Travellers were able to shop around among travel agents for the lowest price.

2.3 The Impact Of Rising Commissions On Industry Structure

Open rate commissions have had a significant impact upon the travel agent industry, upon the way the travelling public views the industry and upon the industry's relationship with the airlines.

Evidence of rising commission expenses facing U.S. carriers providing international service is presented in Exhibit 4. The period, 1974-1976 coincides with the deterioration of the IATA commission resolution previously referred to.

Important changes which are revealed include the following:

- (1) From 1974 to 1976 commissions paid by U.S. carriers for sales of international transportation soared 65.9 percent from \$133.9 million to \$222.2 million.²²
- (2) The recent augmentation in international commission expenses is revealed by the fact that the two year increase was \$88 million while the increase from 1960 to 1974 was only \$87 million.

²¹"How Discounts Bleed the Airlines", Business Week, June 23, 1975, p. 116.

²² Air Transport World, op. cit., Oct. 1977.

- (3) The ratio of international commissions over passenger revenues increased dramatically from 6.31 percent in 1974 to 9.22 percent in 1976.

Rising commission costs have contributed to the lower after tax earnings of major air carriers as have higher fuel and labour costs. Operating statistics presented in Exhibit 5 for all services of Canadian carriers reveal a dramatic increase in traffic commissions from 1974 to 1976. Rising marketing costs such as these have undoubtedly contributed to the poor profitability picture of the two Canadian carriers during this period.

IATA officials have argued that open commissions and price competition in general result in the deterioration of the image of the air travel industry. However, one would not expect support for increased marketing costs from the organization representing the air carriers. With regard to changes in the structure of the travel agent industry, under an open commission structure it appears highly plausible that increased concentration would result because of the economic attraction of offering large volume agencies more advantageous arrangements. In the past the industry has been characterized by easy entry and steady growth. An on-going study of the travel agent industry revealed that at the end of 1976, there were approximately 12,240 conference-appointed agencies in the United States, an increase of 83 percent over 1970. Moreover, the annual dollar volume of sales increased at a substantially more rapid pace, rising 198 percent from 1970 to 1976, an increase of

\$9.9 billion, from \$5.0 to 14.9 billion.²³

However, other statistics tend to indicate an increased market share being captured by the larger agencies. Over the same period of time, the growth of small travel agencies was only 19 percent while medium sized agencies increased 136 percent and large agencies 114 percent.²⁴ The same study also indicated that the dollar volume of sales for individual small agencies actually declined between 1970 and 1976. This too is indicative of the trend toward concentration of sales in the larger agencies

One must, however, be careful not to draw hasty conclusions regarding the cause of industry concentration at the top. Open rate and incentive commissions are not the sole causal factors contributing to the dominance of the large agencies. Indeed, revenues earned from international air travel commissions only account for approximately 25 percent of the sales volume which a travel agency produces.

²³ Louis Harris and Associates, The Character and Volume of the the U. S. Travel Agency Market, Ziff-Davis, New York, April 1977.

²⁴ Small agencies are defined for analytic purposes as those having annual sales of less than \$500,000; medium sized agencies have sales between \$500,000 and \$ 1 million; large agencies have annual sales greater than \$ 1 million.

Exhibit 4

International Travel Agent Commissions
Paid By United States Airlines
1974-1976

	1974		1975		1976	
	1	2	3	4	5	6
Americ.	7.86	6.11%	10.35	6.62%	15.21	7.52%
Braniff	6.05	5.89	7.98	7.60	9.23	7.97
Eastern	13.43	5.72	15.41	5.96	16.87	6.14
N. West	6.50	4.63	13.11	8.42	36.12	18.81
Pan Am	68.27	6.97	83.60	8.27	101.8	9.82
TWA	28.27	6.36	31.91	7.15	37.66	7.73
Western	1.45	4.17	2.13	6.03	2.41	6.68
Total	133.91	6.31%	166.72	7.49%	222.25	9.22%

1, 3, 5, "Commissions Paid To Travel Agents In \$millions.

2, 4, 6 "Commissions As A Percent Of Airline Revenues.

Source: United States Civil Aeronautics Board In
"U.S. Airline Commissions Jump In 1976",
Air Transport World, October, 1977, P.34.

Exhibit 5

Travel Agent Commissions
Paid By Scheduled Canadian Carriers
1970-1976

Traffic Commissions (\$Millions)

1970	24.93
1971	26.16
1972	32.26
1973	37.00
1974	48.79
1975	58.97
1976	68.17

Source: Statistics Canada, Air Carrier
 Financial Statements, Catalogue
 51-206, 1970-1976.

A logical argument concerning the loss of the impartiality which is characteristic of the travel agent has been put forth by opponents of open commission structures (the primary members being the air carriers). They argue that when non-uniform commissions and incentive payment schemes develop, travel agents no longer offer impartial advice to travellers vis-a-vis carrier choice. Moreover, by acting as agents of their principals, the air carriers, proponents of uniform commissions, have argued that travel agents have an ethical obligation to represent each of the principals on an equal basis; under non-uniform rates travel agents, motivated by the economic incentive, direct

traffic to those carriers offering the higher commission.

Alternatively, suboptimal booking, (i.e., selling space on a carrier which does not necessarily provide the passenger with the optimal service characteristics available from the market), would not necessarily occur because the short-term additional revenues earned from diverting traffic to carriers paying higher commissions might not be as great as the goodwill loss caused by suboptimal bookings. Nevertheless, the reliance upon the advice of the travel agent is particularly important in the case of international air travellers who are less familiar than their domestic counterparts in the choice of carriers and gateway cities.

The deterioration of the previously homogeneous international commission structure and the subsequent development of an open commission situation have caused regulatory officials, carrier management and travel agents to search for a remuneration scheme which is generally acceptable.

2.4 Alternative Compensation Schemes

A marked need in the airline industry exists which calls for the commitment of the international airline community to a well established compensation scheme. If left untouched, escalating commission expenses could result in a dramatic alteration in the marketing practices of the international airline industry which may or may not be in the public's best interest. Indeed, concern over this matter on the part of airline management formed the impetus behind an extensive C.A.B. investigation into airline remuneration procedures.

For the purpose of outlining significant advantages and disadvantages of remuneration scheme alternatives, the following three alternatives: net fare, uniform and incentive commission structures shall be analyzed. The regional development incentive commission which is essentially a regulated version of the incentive commission alternative is also considered.

The Net Fare Remuneration Alternative

Under a "net fare" approach, travel agents would not earn a commission from the carriers per se, instead, they would charge passengers outright for their services. Such a system would only be viable as a means of reducing overall airline marketing costs provided that carriers reached an agreement excluding the possibility of unauthorized commission payment. If this were not the case, a highly competitive commission payment situation would emerge under which competitive pressures would force most carriers to pay some commissions.

In theory, the net fare concept appears to be quite attractive from a public policy point of view as well as from the point of view of the carriers. The primary advantage to this approach which is frequently cited by airline conference officials, lies with its reliance upon the market mechanism i.e., the demand by consumers for agents' services, in determining the value of the service performed by the agent.²⁵ With fares set exclusive of commissions, the passenger would

²⁵"Airfare Commissions May Go-IATA Considers Net Fare Policy", Canadian Travel Courier, May 5, 1977.

have the choice of purchasing his ticket either from the carrier or from an agent at a somewhat higher price depending upon prevailing market conditions.

The impact of introducing such a distinctly different remuneration method would most likely have a significant impact upon the structure of the travel agent industry. One could anticipate observing larger firms with higher volumes capturing a larger market share while some smaller firms with lower volumes would probably drop out of the industry. The reason for this stems from the lower charge earned per ticket sold in comparison with the previous standing "closed" commission structure. Another contributing factor to the demise of the "corner" travel agent is its high overhead relative to sales volume.

One might argue that since economies of scale are significant for the retail travel agent industry, it would be in the public's best interest if the less efficient small firms were gradually weeded out and average firm size increased. However it is not entirely clear that small firms are indeed inefficient in performing all tasks required of travel agents.

In order for small agencies to prove to be economically viable business concerns, they would have to specialize in a particular range of services which are not as readily provided by the large agencies. An example of such a specialized service is found in the Canada-Hong Kong travel market. In this market, ethnic travel agents provide a unique range of travel services; an ethnic traveller from Canada may find it to his advantage to seek the advice of a specialist in this field.

The impact of the net fare concept could be more comprehensive than is evident at first glance. If the airline conferences were successful in implementing such a procedure, other modes of passenger transportation would be faced with the decision of whether to follow suit or not.

By retaining commissions, other carriers could obtain a competitive advantage due to the incentive to promote the services of the carrier offering a higher monetary incentive. Nevertheless, with regard to passenger services, inter-modal competition is severely limited especially in the area of commercial or business travel; a trans-Atlantic cruise offers the hurried businessman a poor substitute to a trans-Atlantic flight.

Alternatively, if tour, oceanliner, rail and bus companies were to follow the net fare concept established by the airlines, established agencies would be exposed to a greater degree of risk. Agencies would immediately find themselves without a guaranteed commission rate and instead, exposed to the competitive pressures of a marketplace characterized by price competition.

The effect upon some agencies, particularly upon those located in urban core areas in close proximity to airline operated city sales offices could prove to be disastrous. Many travellers, particularly those from the business community, would be attracted to airline owned and operated city sales offices offering the same transportation services and similar marketing conveniences.

The Uniform Commission Rate Alternative

From the time the C.A.B. found that the fixing of agents' commissions was not adverse to the public's interest in 1947,²⁶ to the recent rejection of the International Air Transport Association's request for an increase in commission levels in 1974, commission levels have been the same for all carriers in the market. This has meant that unless under-the-table dealings were taking place, conference member carriers have agreed to pay agents the same rates of commission for the various types of services sold such as domestic point-to-point, international point-to-point and inclusive tours. For the purpose of analyzing the various remuneration alternatives, the possibility of returning to a uniform commission level should be considered.

One of the major advantages of requiring all carriers to provide agents with the same level of remuneration which accrues to the carriers is the stability of sales revenue due to the lack of fluctuation in commission levels. Uniform commissions which are closed and not subject to change over a period of time have, since their introduction in 1947, received the support of the airline conferences. Moreover, polls have revealed that travel agents in the United States favour uniform rates of commission for domestic as well as international air transportation. In May of 1975, a poll of A.S.T.A. members with 689 respondents resulted in an affirmation of single commission structures:²⁷

²⁶ United States, Civil Aeronautics Board, op. cit., p. 1.

²⁷ Ibid., p. 97.

From an economic and marketing point of view, do you believe that single, or differential commission structures and levels should apply to the sale of domestic versus international air transportation?

Single	67 %
Separate	33 %

One should be aware of the difference between higher commission rates and open commission rates. Although it has been argued that the carriers will incur higher commission expenses under open commissions (i.e., under conditions where carriers are free to set the commissions they are willing to pay agents), it is conceivable that closed commission expenses for the industry as a whole could be greater than open commission expenses even though some carriers, especially those offering incentive commissions, would incur higher commission expenses under open commission rates.

Another significant advantage attributed to uniform commission levels concerns the maintenance of the impartiality of the agent in its fiduciary relation to the principal. Travel agents are not immune from being swayed by the economic incentive which differential commissions offer. One of the major reasons why travel agents are able to maneuver passengers to the carrier paying the highest commission is that most passengers rely upon the advice of travel agents with regard to carrier, hotel, tour package and frequently ground arrangement choice. Indeed, according to a survey of travel agents in the United States, 72 percent of the personal pleasure travellers and 55 percent of the business travel clients rely upon travel agents

in the selection of carriers.²⁸

As the present "commission war" has shown, some agencies have altered their sales patterns in accordance with the higher commissions offered by particular carriers in particular markets.

It has been argued by opponents to non-uniform commissions that the public is at no disadvantage and passengers are not ill-served by non-uniform commissions. The argument runs along the lines that if passengers are ignorant of the effects of distorted incentives upon services received, what they do not know cannot hurt them. Katherine Kent, Administrative Law Judge, in hearings concerning uniform commission payments to travel agents has rejected this argument in arguing that:

...when a passenger consults an agent because of his own lack of information as to carriers and schedules and has confidence that the agent will deal with him fairly and impartially and the agent does not fulfill his obligations, the passenger is disserved whether he knows it or not.

By retaining the impartiality of the agent, the individual air traveller, who may very well be ignorant of all of the travel options available to him, benefits from a higher level of customer service.

Another compensation scheme which should be considered by regulatory agencies as a viable alternative is the incentive commission. The most utilized forms of incentive commissions are volume and destination incentives. Under the former, carriers offer agents higher commissions for sales volumes exceeding

²⁸Louis Harris and Associates, op. cit., April 1973, p. 19.

certain preestablished passenger traffic levels. Preestablished schedules of commission payment are based either on passenger volume levels or on sales revenue levels with individual carriers. Under the latter, carriers offer agents higher commission payments for booking to certain locations which, for one reason or another, the carrier is attempting to promote.

One of the major advantages to incentive commissions rests with the flexibility which airline management obtains from the active manipulation of this marketing variable. This facilitates the stimulation of individual market segment demand. For example, by employing a destination incentive on a particular route, marketing efforts can be directed toward stimulating increased traffic on routes where competitive retaliation would not be significant. However, this "micro" view is in need of a broadening of scope; the impact of incentive commissions upon the airline industry has proven to be substantial as has been shown in Exhibits 4 and 5.

Appendix 1 presents samples of competitive passenger commission filings in the United States. In it are shown a multitude of volume and destination incentives as well as bonuses offered American travel agents in March of 1978.²⁹ One should note the vast differences in incentive schemes as well as the large number which carriers must be aware of in order to maintain their competitive positions in the marketplace.

The issue of whether the public should have access to rates

²⁹Summary of Competitive Passenger Commission Filings in the USA, CP Air, Industry Affairs, March 1978, p. 1.

of commission paid middlemen has received some attention in the U.S. in recent years. In fact, a policy statement by the Ford administration in the United States clearly expressed the need for public information on this subject. The policy statement reasoned that in order to "help ensure consumer awareness and to permit the C.A.B. to take commission costs into account in determining total carrier costs as a basis for fare decisions, carrier commission structures should be filed for public inspection at the Board."³⁰

The C.A.B. ordered carriers to begin filing detailed reports of all commissions and other compensation paid travel agents and tour operators in early 1976. The rationale underlying the Board's order is essentially that because commissions are part of air ticket prices, the public should be made aware of the rate of commission which middlemen earn.

Aside from increased airline management control over the pricing decision variable, incentive commissions require management to maintain a constant surveillance of changes in commission levels and individual airline incentive schemes. From an industry-wide perspective, additional emphasis upon setting appropriate commission levels entails an increase in marketing costs which may eventually be shifted to the consumer.

Travel agent association officials have argued that the higher rate of commission earned from incentive commissions can be used to the public's benefit by providing additional promotional activities. Moreover, one might argue that public

³⁰United States, Ford Administration, International Air Transportation Policy of the United States, September 1976, p. 26.

policy objectives could better be achieved if government regulatory bodies directed commission structures in such a manner that certain groups of travellers received additional promotional benefits. However, a much more visible approach, that of altering prices, is a more efficient means of implementing price discrimination and the subsidization of one group by another. One reason for this lies with the fact that different groups depend upon travel agents more than others. For example, it is generally accepted that pleasure travellers rely more heavily upon the services of travel agents than do businessmen.

Incentive commissions which offer agents higher commissions for booking to certain destinations or for sales volumes which exceed certain preestablished levels should not be confused with the "open" commission alternative compensation scheme considered in this thesis i.e., such would be the case with the total deregulation of commissions paid by carriers to middlemen; an open commission situation is not necessary for incentive commissions to be offered. Incentive commissions might be regulated so that marketing costs to the airlines would not increase substantially or at least not as much as they have since the development of open commissions as documented in the previous section.

Further insight into the effect which incentive commissions have had on the international trunk carriers is revealed in Exhibit 6. As shown in the exhibit, passenger commissions as a percent of revenues for international carriers increased from 5.81 percent in the first quarter of 1975 to 8.47 percent in the

third quarter of 1977. Nevertheless, this increase in average commission rates has been augmenting at a declining rate.

Exhibit 6

Passenger Commissions as a Percent of Revenues (International Trunk Carriers)

<u>Date</u>	<u>Commission Level</u>	<u>Percentage Increase Over Previous Year</u>
March 31, 1975	5.81 %	
June 31, 1975	6.01	
Sept. 31, 1975	6.40	
Dec. 31, 1975	6.86	
March 31, 1975	7.43	27.9
June 31, 1976	7.86	30.8
Sept. 31, 1976	8.25	28.9
Dec. 31, 1976	8.42	22.7
March 31, 1977	8.32	12.7
June 31, 1977	8.40	6.9
Sept. 31, 1977	8.47	2.7

Source: IATA Agreements Concerning Agency Matters--Uniform Commission Rates,
Washington D.C.: March 15, 1978, p. 60.

Incentive commissions have been cited as the bulk of the cause behind increasing commissions in recent years. This fact tends to indicate the highly competitive nature of the marketing battle among the carriers to attract the large-volume and selected-volume agencies. More importantly, an open commission structure which emphasizes incentive commissions tends to shift

control of a larger segment of the market to the volume specialists to the detriment of the smaller agencies.

Although owners of small travel agencies would not agree, from an economic efficiency point of view, it might be more advantageous in an industry marketing a highly homogeneous product such as air transportation for large firms to capture a greater share of the market. Observers of the travel agent industry have noted that the industry has become much more concentrated in recent years. Since incentive commissions tend to reinforce this concentration, the Canadian Transport Commission must reach a decision as to whether permitting carriers to offer agents incentive commissions is in the public's best interest.

The Regional Development Commission Alternative

Under the present uniform commission structure prevailing in Canada, travel agents in Whitehorse, Yukon Territory, earn the same rate of commission as do travel agents in Toronto. Agents earn the same rate of commission based on the published airfare irrespective of the community where they are situated whether it be an isolated northern outpost or a thriving southern metropolis.

Airfares to the North from the major Canadian centres of population are generally higher per journey than the price of the average ticket in southern Canada. This is because it costs northern carriers more to provide transportation services. Moreover, average distances between centres of population are greater. All of this implies that the average commission earned

on the sale of an air journey is higher. Nonetheless, travel agent operating costs, especially the labour portion, are generally much higher in northern communities than in the South.

As is frequently the case when a proposal is put forth calling for the subsidization of a particular geographic region, government officials and taxpayers ask how is a subsidy for northern residents in the interest of the country as a whole? Answers to this question would have to be found if higher commissions were allowed to be paid to travel agents in northern communities because unless airfares were raised on northern routes, the net result would be a subsidy of airline marketing costs in northern communities.

The rationale underlying the need for higher rates of commission in the North is found in the great importance which air transportation plays in northern development. One authority on the subject has stated that "In most new remote communities air transportation is vital... It is often the only practical way for relatively permanent residents to travel to larger centres for recreation, shopping and other purposes."³¹ If regional development commissions which allowed agents to earn higher rates of commission on their sales were approved by the Canadian Transport Commission, one could then anticipate profits to rise and new firms to enter the industry offering passengers a wider range of travel counselling services. There is little

³¹K. M. Ruppenthal, The Centre for Transportation Studies, University of British Columbia, Transportation Needs and Availability in North Coastal Communities in British Columbia, (Vancouver, B. C.: Centre for Transportation Studies, 1978)

doubt that higher commissions in northern communities would ameliorate northern travel agency conditions by providing additional incentives to small businesses to offer a wider range of services.

If travel agents are to earn higher commissions than their associates in southern population centres, then the issue of by how much should northern commission rates exceed southern commission rates would have to be resolved.

One alternative proposes that average cost differences between agencies operating in southern cities and agencies in northern cities be apportioned in such a manner that higher commission earnings could offset the higher costs of operation in northern areas. One disadvantage with such a proposal is that a great deal of variation in operating costs of northern agencies poses the problem of non-uniformity. Another area of concern is that cost determination procedures are costly to implement and since no single costing method is necessarily the best costing method, government regulatory agencies and travel agents would have to come to a consensus before any progress in this area could be made.

Before blindly accepting a proposal calling for regional development commissions, additional problems with implementation should be considered. Clearly, some degree of animosity could be expected from travel agents not classified as northern travel agents. And of course, the carriers which tend to favour stimulating traffic through high volume, specialty agencies located in urban centres would most likely object to the additional cost imposed by higher commissions.

In essence, what policy-makers are faced with in this situation is the fundamental question of whether northern development should be subsidized by the producing areas in the South. Higher commissions in the North imply a subsidy of northern sales intermediaries by the carriers and possibly by agents in urban southern Canada.

CHAPTER 3 INDUSTRY REGULATION

3.0 The Process Of Entry

The establishment of a successful travel agency requires a stable financial backing and knowledge of a particular segment of the travel industry. In this chapter, questions such as the following are addressed: "What is the extent to which government has regulated the travel industry?"; "How have provincial government registration requirements affected the industry?"; One ought to also ask, "How has the travelling public benefited or suffered from the protection offered by provincial government legislation?"

Individuals or aspiring entrepreneurs seeking to establish new travel agencies in Canada find that similar to many other regulated transportation industries, entry requirements are not insignificant and legal and financial barriers must be surmounted before profits are forthcoming and fringe benefits enjoyed. Generally speaking, it is no longer possible for entrepreneurs to open "whole in the wall" travel agencies selling space on non-IATA carriers, at least not in British Columbia and in those provinces and states with travel services legislation.

The most prestigious certification which a travel agent can receive is the seal of approval from the International Air Transport Association. Certification from this organization is highly desirable because the vast majority of international airlines belong to IATA and international ticket sales make up a

large portion of total airline ticket sales by travel agents in Canada.

A series of steps must be followed before obtaining International Air Transportation Association (IATA) and Air Traffic Conference (ATC) approval and of course, a provincial government licence to market travel services. First, the newcomer to the travel industry must satisfy a list of prerequisites before becoming licenced to sell travel services. After satisfying financial character requirements, the debutant is then ready to be licenced and begin contributing to the provincial travel services compensation fund designed to provide redress to consumers in need. However, this is only the beginning of the requirements facing the new agent. Receiving provincial government approval in no way entitles the licensee to sell space on IATA or ATC carriers. Conference recognition is only conferred upon the agent after numerous requirements have been met.

3.1 Airline Conference Recognition Of Travel Agents

Long before provincial legislation was enacted dealing with travel agents, IATA had established a detailed set of requirements for agency approval. One should, however, note that provincial government legislation is much more comprehensive as it encompasses tour wholesalers retail travel agents and non-profit organizations engaged in the marketing of travel services. Due to the lack of comprehensive entry requirements, it was possible for tour wholesalers to sell space on air carriers along with ground transportation and hotel

accommodations. All too often, travellers were left with worthless tickets or even worse, were stranded abroad. In such cases, air carriers frequently volunteered their services to stranded passengers or honoured their tickets even though no revenue was collected from the insolvent travel firm.

In Canada, agencies which have previously been established but not yet approved, must apply to the Agency Investigation Panel, a division of IATA. This panel administers a programme whose objective is that of assuring that agency outlets used by IATA carriers are capable of providing accurate and dependable service to the public. Other objectives of the programme include ensuring that adequate financial controls have been taken and that unauthorized commission payments are eliminated.³² Indeed, one of the binding agreements which IATA carriers must agree to in order to retain membership in the organization is the restriction of commission payments only to those agents which have been approved by the IATA machinery.

The specific IATA requirements for establishing a new agency are as follows:³³

- (1) Sponsorship: An agency must be sponsored by one of the member airlines. However, no agency is accepted if it is owned partly or wholly by an air carrier.
- (2) Time in Business: An agency must be able to show that it has been established, staffed and has been doing business for at least six months.

³²Brancker, J.W.S., IATA and What It Does - A. W. Sijthoff, Leyden, The Netherlands, p. 60.

³³Audrey Saunders, International Air Transport Association, Agency Investigation Panel, Correspondence, March 25, 1977.

- (3) Sales Volume: The agency must have the ability to generate business not considered to be presently reaching the airlines. The agency must provide a resume of sales productivity for sales on non-IATA carriers.
- (4) Experience: The Agency Investigation Panel uses discretionary power for special circumstances but in general, minimum levels of experience are required for two key managers in the travel agency; the manager of the agency must have had two years of full-time experience in an IATA approved agency or an IATA carrier in "creating, generating and promoting passenger transportation, sales and services". In addition, another agent must have had at least one year of experience in international airline ticketing and reservations with an approved agency or carrier.
- (5) Promotional Activities: The applicant must demonstrate to the panel that the agency has the ability to promote the sales of international air transportation.
- (6) Premises: The premises must be devoted exclusively to the promotion and sale of air passenger transportation and related services. The premises must also be clearly marked as a travel agency. Photographs depicting the appearance of the agency must be submitted to the panel.
- (7) Financial: The applicant must provide an audited balance sheet as well as a bank statement verified by the applicant's banker. The firm's working capital must exceed \$15,000. Net worth in the case of partnerships and proprietorships and paid in capital in the case of corporations, must not be less than \$20,000.
- (8) Industry Need: One of the most important stipulations set forth by the panel is the need requirement because this effectively gives the Agency Investigation Panel the power to reject an application in a particular locale thereby avoiding the dilution of sales revenues of existing IATA approved agencies.

When evaluating individual applications, the Agency Investigation Panel uses discretion by taking into consideration differing local market conditions. For example, the requirements for management experience and physical appearance of the

premises would most likely be relaxed for the frontier town of Williams Lake, B.C., whereas they would be held to strictly in cosmopolitan Montreal where international airline sales offices are presently saturating the downtown area.

The Air Traffic Conference of America (ATC), an airline conference affiliated with the Air Transport Association of America and composed of U.S. domestic carriers with associate provisions for the two major Canadian carriers has developed similar standards for individuals seeking to establish travel agencies which would engage in the sale of space on ATC carriers. Similarly, the Air Transport Association of Canada (ATAC), a conference of Canadian carriers has developed similar entrance criteria. Even though the three conferences use similar criteria for the evaluation of new applicants, they have yet to combine resources and eliminate the necessity of applying to separate organizations in order for Canadian travel agents to sell travel space on domestic as well as international carriers which are members of the two bodies.

Even though conference entry requirements have not diminished in rigidity, the number of conference appointed agencies has witnessed phenomenal growth over the past decade. In the United States, at the end of 1976, there were approximately 12,240 conference-appointed agencies. This represents an increase of 83 percent over the approximately

6,800 agencies which were in business in 1970.³⁴ The annual volume of sales of these agencies in 1976 was \$14.9 billion, or approximately three times the 1970 level.

In an industry with such an impressive record for growth, it is little wonder that entrepreneurs both qualified and incompetent have been attracted to the industry. The number of new entrants to the industry has created an acute need for public policy makers to decide whether more stringent regulation of the industry should be forthcoming. This issue is addressed in the section which follows.

3.2 Causes Of Agency Failures

In early 1977, before travel agency legislation was made law in British Columbia, a Hawaii-based tour operator closed the doors of its Vancouver office depriving as many as one thousand British Columbians of both their long awaited winter holidays and approximately \$300,000.³⁵ According to local newspaper reports³⁶ the failure of H. G. Haina and Associates of Honolulu placed a great deal of pressure on the carriers which were to

³⁴The Character and Volume of the U.S. Travel Agency Market: 1976, Louis Harris and Associates, Inc. Pp. 5-6, cited in IATA Agreements Concerning Agency Matters-Uniform Commission Rate, Docket 28672 U.S. Civil Aeronautics Board, March, 1978, p. 19.

³⁵Information on recent developments concerning Canadian travel agents is discussed in "Licensed Leisure", The Financial Post, March 26, 1977, p. T-3, a special supplement on the travel industry.

³⁶"Sun Not Down Yet on Hawaii Trips", The Province, February 8, 1977, p.27.

provide transportation services to Haina customers and on the travel agents which were involved in the marketing of the bankrupt firm's tours in Hawaii. In fact, one major department store owned travel agency agreed to unconditionally guarantee the holidays of twenty-three of its customers. A spokesman for Northwest Orient Airlines expressed his company's willingness to honour all tickets issued on his airline for inclusion in Haina tour packages. Underlining the importance of travel industry regulations from a humanitarian point of view was the fact that sixty Victoria-area old age pensioners were among the victims of the folded tour wholesaling firm.

Events such as this have created a rallying point for those interested in protecting the interests of consumers of travel services through the licensing and regulation of travel agents and tour wholesalers. Actually, the occurrence of unfortunate events such as this has had much broader implications: politicians and the travelling public have started to question the usefulness of travel agents as the marketers of travel services.

A number of outstanding factors may be pinpointed as the cause of the failure of travel agent legislation. Among the most common maladies facing the industry is a lack of sufficient working capital to support the drain on funds during cyclical swings in the travel industry business cycle. Another contributing factor to bankruptcies rests with a lack of business management experience. Before travel agent legislation came into effect, entrance into the industry was relatively straightforward with no significant barriers confronting

individuals aspiring to sell tickets on non-IATA carriers and ancillary travel services such as tours and hotel accommodations. The industry could appropriately be characterized as efficient with a sufficient degree of competition among small as well as large firms marketing similar products.

Alternatively, there is a cost to the public associated with this type of an unregulated industry. Since the jet boom began more than two decades ago, thousands of travellers have been stranded or were not able to start their journeys due to the bankruptcy or fraud of travel agents.

Travel firms specializing in inclusive air tours including air and land transportation as well as hotel accommodations have shown themselves to be much more susceptible to business failures than are retail travel agents. Therefore, one would expect travel wholesalers to be included in most provincial legislation regulating the travel industry. Nonetheless, one should note that if a passenger makes his air travel arrangements for travel on an IATA or on an ATC member carrier, the air travel portion of the services purchased shall be protected even if the individual travel agent becomes insolvent.³⁷

Alec Burden, the Registrar of Travel Agents for British Columbia has provided some insight to the cause of travel agent failures by outlining the characteristics of agencies likely to

³⁷George Buchannan, Air Transport Association of America, Testimony before the U.S. Senate Subcommittee on Foreign Commerce and Tourism, Nov. 18, 1971.

fail:38

- (1) The duration of business has generally been less than two years.
- (2) The staff is inexperienced in the travel industry.
- (3) The firm is short on operating cash.
- (4) The agency has financial connections with other agencies in financial trouble.
- (5) A high proportion of their business will have been in air travel.

Due to the frequent occurrence of shoddy arrangements through unregulated travel agencies, consumer activists prompted politicians in Canada and the United States to enact legislation to protect the purchasers of travel services. Similarly, travel industry legislation was designed to protect existing agencies by creating barriers to entry.

3.3 Travel Agent And Travel Industry Legislation

As the result of efforts by a highly organized travel agents association in Ontario, the Ontario Travel Industry Conference (OTIC), the Province of Ontario passed legislation in December of 1974 regulating the operations of travel agents and travel wholesalers. These efforts were motivated as much by the desire to promote an image of professionalism within the industry as they were to protect the consuming public.

Ontario's Act which is commonly referred to as the Travel Industry Act, establishes a special office under the Ministry of Consumer and Commercial Relations. One of the primary objectives of the Act is to register all travel agents meeting the established minimum requirements. These minimum requirements are

38"20 to 30 Travel Agencies Expected to Fold", The Province, June 1, 1978, p.4.

designed for the purpose of eliminating the so-called "fly-by-night travel agents", hence, requirements related to responsibility and ability to maintain a viable business enterprise in an honest manner are included. Specific prohibitions have been established restricting individuals with fraudulent backgrounds from becoming licenced.

The Act clearly outlines the requirements for travel agents in Ontario seeking to sell travel services to the public. The mobility of travel agents is somewhat more restricted under the Act; the Registrar is empowered under the Act, to maintain records of travel agents and travel agencies. If, for example, an agent wishes to move from one employer to the next, he must notify the Registrar. Furthermore, the travel agent is only allowed to work for one employer at a time.³⁹

Audited financial statements indicating the financial soundness of the travel agency must be supplied to the Registrar. With the power of inspection, the Registrar may audit the financial records of travel agencies if he so desires. Investigations are however, only possible if the Ministry of Consumer and Corporate Relations has reason to believe on reasonable grounds that an agent has violated any of the provisions of the Act or alternatively has committed an offense under the Criminal Code of Canada. An additional degree of protection is provided by the Act by a special clause dealing specifically with deceptive and false advertising. The marketing

³⁹Ontario, Statutes of Ontario, "The Travel Industry Act, Chapter 115:15, P. 1061.

of tours has proven to be particularly susceptible to deceptive advertising and therefore, additional surveillance on the part of the Registrar may be deemed to be in the best interest of the travelling public.

The Ontario Travel Industry Act requires all travel agents and travel wholesalers to post a bond with a face value of from \$5,000 to \$25,000 depending upon their sales volume.⁴⁰ Moreover, an annual payment to the compensation fund is required which is directly proportional to the sales level. A compensation fund funded by travel agents contributions is highly desirable for consumer's protection particularly for the travel industry for a number of reasons. First of all the risk of business failure resulting from lags between cash inflows and outflows and poor cash budgeting is relatively high in comparison with other small businesses of equivalent size with a similar level of fixed costs. Secondly, the ratio of total revenue to fixed costs is relatively high for travel agents; combining this with seasonal fluctuations in sales levels can imply significant exposure to business risk and large sums of money resting in the coffers of travel agents while in transit from traveller to carrier.

British Columbia followed the lead of Quebec and Ontario and established its own Travel Agents Registration Act which came into force on February 21, 1978. The Act is revealed in its entirety in Appendix 2. Although modelled closely after the

⁴⁰"Licensed Leisure", The Financial Post, March 26, 1977, pp. T1-7.

Ontario Act, British Columbia's Act has some important differences which its authors believe provides additional consumer protection. For example, an important feature of the Act is found in its provision of protection for British Columbia consumers whose travel agents deal with out-of-province wholesalers.⁴¹

One of the most convenient means of compensating travellers for their losses as the result of a travel agent failure is to establish a special compensating fund expressly for that purpose. Such is the case with the British Columbia Act. A Travel Assurance Board comprising representatives from consumers, the travel industry and the Ministry of Consumer and Corporate Affairs administers a Travel Assurance Fund, a special trust fund under the government's general revenue fund against which consumers may make claims if they fail to receive travel services for which they have paid.

The fund may reach a maximum size of \$700,000. Cash reserves of the fund are accumulated through contributions of agents on a pro-rata basis.⁴² Rair Mair, B.C. Consumer and Corporate Affairs Minister estimated that "the number of cases in which the fund will be needed will be small, but each case could involve huge amounts of money."⁴³ Compensation is granted to those who have suffered direct economic loss as stated in

⁴¹News Release, British Columbia, Ministry of Consumer and Corporate Affairs, Jan. 30, 1978. P.30.

⁴²Ibid., p.30.

⁴³"B.C. Travel Operators Welcome Registration Provisions", The Province, Feb. 12, 1977, p. 10.

Section 17 of the Act:⁴⁴

- (1) A person who has suffered direct economic loss by reason of

(a) the insolvency or bankruptcy of a travel agent or a travel wholesaler registered under this Act, or

(b) failure to collect money ordered by a court to be paid by a travel agent or wholesaler registered under this Act after reasonable execution proceedings have been attempted, or

(c) such other circumstances as may be prescribed may, subject to this Act and the regulations, apply for compensation from the fund.

In order to enforce the Act properly, specific penalties have been provided for in the legislation. Also, an early detection system requiring agencies to file annual financial reports with the Registrar has been provided for in the Act.⁴⁵ Moreover, if the Registrar suspects that an agency has not been adhering to the requirements of the Act, an investigation of the particular agency in question under the auspices of the Registrar may be undertaken.

One of the alleged benefits of travel industry legislation is that it improves the public's image of travel agents and tour operators. Although one might expect travel agents to be somewhat apprehensive when faced with legislation curtailing managerial freedoms, a great deal of approval was evident in

⁴⁴British Columbia, British Columbia Statutes, "Travel Agents Registration Act, Chapter 22, 1977.

⁴⁵"Summary of Proposals Pertaining to Travel Services Legislation", Douglas K. Harrison, February 1977. (mimeographed)

British Columbia subsequent to the introduction of the Act. The president of the British Columbia chapter of the Canadian Society of Travel Agents indicated particular approval of registration provisions which require "some professionalism" from travel industry participants.⁴⁶

As with many government imposed insurance schemes, a certain degree of debate developed over the issue of who shall pay for increased consumer protection; should it be the traveller, the retail agent, the wholesaler, the carrier or as is so often the case, the taxpayer?

Following the enactment of the B.C. Travel Agents Registration Act, retail agents represented by the Association of Travel Agents of British Columbia expressed some concern that Section 8 of the Act⁴⁷ holds retail agents liable for all consumer claims which have not been covered by the travel fund.⁴⁸ Essentially, this implies that retail travel agents are not exempt from joint and several liability and more importantly, consumers of travel services are entitled to repayment of money which they paid. The Act therefore requires the travel industry to bear the burden of the cost of administering the act.

The impact of travel industry legislation with mandatory

⁴⁶Op. Cit., The Province, p. 10.

⁴⁷Section 8 of the British Columbia Travel Agents Registration Act is revealed in Appendix 1.

⁴⁸"If B. C. Fund Runs Out, Agents May Have to Cover Client Losses", Canadian Travel Courier, No. 12, April 7, 1977, p.1.

compensation funds upon the approximately 400 firms which registered following the enactment of the legislation might appropriately be compared to legislation requiring firms to insure themselves against bankruptcy. The burden of additional costs must be borne by firms within the industry but benefits are derived from the additional protection which consumers enjoy.

The legislation uses minimum financial requirements as a safety device to protect the public from floundering agencies and tour operators. On-going financial standards must be maintained by agencies in British Columbia if their registrations are to remain valid. According to Regulations under the Travel Agents Registration Act, sole proprietorships can have their registration certificates cancelled if they develop a negative net worth or working capital position; and corporations can lose their certificates if they fail to maintain a net worth position of at least \$15,000.⁴⁹

Financial requirements such as these cannot be maintained without costs being incurred by the firms which are most directly affected. From the individual firm's point of view, a working capital position which is larger than what would be the case without legislation implies an opportunity cost especially if short-term debt is relied upon heavily to finance growth.

Some degree of resentment to the newly introduced legislation was evident subsequent to its introduction in

⁴⁹British Columbia, Ministry of Consumer and Corporate Affairs, "Regulations under the Travel Agents Registration Act", May 1977, p.4.

British Columbia, particularly among the smaller firms. In the interest of countering the present industry trend toward concentration, one must question the appropriateness of the initial \$400 per office registration fee as small agencies may find their financial resources strained to meet the initial application fee hurdle. Perhaps legislation designed to stimulate the growth of small agencies such as a graduated or progressive tax structure would better serve the interests of the travelling public. Moreover, costing studies designed to measure the cost of selling an airline ticket would be useful in determining whether it is more costly or less costly to rely upon the services of an independent travel agent as opposed to an airline owned city sales office.

Due to various requirements of the Act which could not be met, two or three companies were reported to have dropped out of the industry shortly after the registration deadline.⁵⁰ One can only hypothesize as to whether these agencies would have exposed the public to an excessive degree of risk of business failure. Whatever the case may be, travel industry legislation creates additional barriers to entry for future business firms and hence tends to strengthen the grasp of the market of established firms.

Another potentially troublesome section of the Act centres around the unlimited coverage of travel wholesalers whether they be based in British Columbia or not. David Hordouin, of

⁵⁰"Twenty to thirty more travel agents expected to fold", The Province, June 1, 1978, p.4.

B.C. based Suntours, a tour wholesaling firm, has pointed out that it would be possible for a wholesaler to operate offshore, i.e., outside of the province without contributing to the compensation fund and still benefit from the consumer protection offered by the Travel Assurance Fund.⁵¹ The reason for this is that a registered retail agent can sell tours packaged by any wholesaler in the world with travellers purchasing those tours protected by the compensation fund.

The implication of this law for the provincial travel industry could be significant in the future if compensation fund contribution requirements increase significantly above their present level. British Columbians could easily witness the gradual exodus of travel wholesalers to provinces with either less stringent regulations or no regulations at all.

3.4 Consumer Protection From The Risk Of Bankruptcy

Small travel agency firms which have not been established for a sufficient length of time are highly sensitive to the lag between carrier payment and the collection of receivables. Due to the fact that air carrier conferences, tour operators and hotels require prompt payment and competitive pressure may force agency credit managers to extend credit to commercial accounts to a dangerous degree, agencies can easily find themselves highly exposed to the risk of bankruptcy.

Of the importance of airline ticket sales payment dates to

⁵¹"B.C. Act Insures the Whole World, Wholesale Group Tells Government", Canadian Travel Courier, April 7, 1977, p.2.

travel agents there is little question. For most travel agencies, airline ticket sales comprise the bulk of revenues earned. The IATA Bank Settlement Plan requires travel agents to remit funds to settlement banks on a bimonthly basis. Agencies with a high percentage of commercial sales (which generally implies delays in cash inflows) can easily be confronted with insolvency when declining sales levels are combined with the payment requirements of individual domestic carriers and the IATA clearing bank. This problem is accentuated when retail agents are required to provide travel services to clients in the case of the failure of wholesalers.

The minimum working capital requirements of the Travel Agents Registration Act combined with the protection offered the travel agent by the Travel Assurance Fund, substantially reduce the exposure to default faced by the agent with a large proportion of its sales through tour wholesalers. According to provisions of the Act, individuals as well as travel agents may make claims against the Fund. Therefore, protection is afforded both consumers and agents at a cost which has its primary impact upon travel agents because in Canada, for the most part, they are not able to strongly influence the rate of commissions which carriers pay.

CHAPTER 4 COMPETITION FOR MARKET SEGMENTS

4.0 Airline Reliance Upon Travel Agents

Travel agents play an essential role as marketing channel members providing services to both passengers and carriers of various types. The airline industry relies heavily upon the travel agent industry to provide travel consulting services and ticketing without bias as to carrier. For the most part, travel agents depend heavily upon air travel to provide them with commission earnings. Indeed, according to a 1976 survey of 708 conference appointed travel agencies, air travel accounted for 63 percent of the total travel sales revenue.⁵²

Essentially, the function of the travel agent is that of facilitating travel arrangements for the traveller. The geographic location of the agency alone can increase the convenience for the customer in purchasing his ticket and making travel arrangements. The traveller avoids ticketcounter queues at the airport. Moreover, clients receive personalized attention which usually extends beyond merely booking a seat on a flight and making a hotel reservation. Many travellers develop effective lines of communication with individual agents which facilitates determining the needs of the traveller. This type of personalized attention, which is very common between agent and client does not, as a general rule, develop as easily between

⁵² Op. cit., Louis Harris and Associates, 1977, p. 10.

airline ticket sales personnel and airline customers. One proponent of travel agents has remarked that the travel agent will "use his experience and knowledge to synthesize the best combination of travel services offered to suit the needs of the individual or group."⁵³

Another important function performed by the travel agent is the organization of packaged tours or as is more often the case, retail travel agents market tours which have been organized and packaged by tour wholesale companies. Similarly, wholesale travel firms frequently own subsidiaries which are active participants in the retail travel business. The Louis Harris survey revealed that 30 percent of the agencies surveyed were involved in the wholesale trade to some degree.

One advantage which the commercial traveller may derive from purchasing air travel services from a travel agent in comparison with an airline operated city sales office, is the availability of commercial credit. Travel agencies specializing in the commercial trade tailor credit arrangements to meet the needs of individual firms. Such agencies are often times overburdened with accounts receivable and were it not for provincial government legislation which establishes minimum working capital requirements, many would become insolvent. Competition between carrier and travel agents for the very important commercial travel market segment has taken on a new dimension subsequent to the introduction of electronic reservations systems (ERS), to travel agencies. The next chapter

⁵³R. Ellis, "Airline v. Agent", Aeroplane, Aug. 14, 1968, p. 15.

of the thesis addresses this issue and considers its implications for the future of the industry.

Airlines have come to be increasingly reliant upon the travel agent industry despite spiralling commission expenses. Due to IATA prohibitions, member airlines have refrained from equity involvement in travel agencies. Moreover, there has been no widely noticeable trend to rapidly augment city sales office capacity; instead, greater emphasis has been placed upon marketing through travel agencies. An excellent example of the unique role which travel agents play may be found in the ethnic communities where carriers have proven themselves to be ineffectual in attracting minority group members to purchase directly from the carriers through airline operated city sales offices. This statement is based upon the observation of a strong travel agent industry within various ethnic communities in Canada.

4.1 Ethnic Markets

Within the ethnic communities of large North American cities, ethnic travel agencies flourish due to a variety of reasons. First, sufficient demand for air transportation services exists because strong familial ties with relatives abroad are still present, especially among communities of new immigrants. Secondly, ethnic agents are familiar with the language and customs of ethnic community members. Indeed, some travel agencies staffed by new immigrants are more familiar with minority group language and customs than they are with the language and customs of the host country. Thirdly, under the

present remuneration scheme in effect in Canada, it costs ethnic community members no more to purchase from an ethnic agent than it does to purchase from an agent or carrier less familiar with ethnic attitudes and customs.

The ethnic travel agent can be defined as an agency which devotes the majority of its resources to servicing travellers from a particular ethnic group. Sociologists define the ethnic group as a group consisting of people who conceive of themselves and are regarded by others as belonging together by virtue of common ancestry and a common cultural background.⁵⁴

Alternatively, one might use language as a criteria by which ethnic travel agents could be identified. The reliance upon foreign languages by ethnic agents and their clients is one of the factors which strengthens the ties between the two groups and makes entry into the ethnic market by non-ethnic group members difficult.

Chinese Travel Agencies In Vancouver

Approximately 25 Chinese travel agencies compete for the bulk of the Chinese ethnic market in Vancouver.⁵⁵ According to 1976 census information, 45,385 or 3.9 percent of the 1.17 million people in metropolitan Vancouver gave Chinese or

⁵⁴Society Today, Rodney Stark, editor, Delmar, Calif.: CRM Books, 1973, p. 528.

⁵⁵Agencies were selected from British Columbia, Ministry of Consumer and Corporate Affairs, Office of the Registrar of Travel Agents, Registered Travel Agents and Wholesalers as of February 21, 1978, (unpublished document).

Japanese as their mother tongue.⁵⁶ The majority of these are of Chinese origin. Due to the relatively large number of travel agencies specializing in a particular market segment, the level of competition is rather high. Evidence of this competition has surfaced in the form of reports of illegal discounting by oriental agencies. One oriental agent recounted that at one point during a recent price war, price levels reached a point so low that receipts from ticket sales were below standard ticket prices less commissions implying that travel agencies were incurring a loss on ticket sales assuming that illegal overrides were not being paid.⁵⁷

Special Services Offered To Ethnic Customers

Ethnic clients can obtain a unique range of services from agents in their communities which are not as readily available elsewhere. The ability to communicate in the language of the ethnic group member is but one of the important services offered by agents. Travel consultants employed in ethnic agencies are often times familiar with popular destinations of ethnic clients. Indeed, ethnic agencies tend to have sales patterns which emphasize a limited number of ethnic destinations.⁵⁸

⁵⁶Canada, Statistics Canada, 1976 Census of Canada, Catalogue 92-821, February, 1978.

⁵⁷Interview with Patrick Wang, Reeds Travel, Vancouver, July, 1978.

⁵⁸This fact was revealed in discussions with CP Air Marketing Managers, in particular, Roger Pike, Sales Forecaster, Vancouver, February, 1978.

Aside from route familiarization, ethnic agents understand the cultural attributes of their clients and may be better prepared to accommodate the desires of ethnic clients. Ethnic agents with contacts within ethnic community organizations are more likely to succeed in developing tours of interest to ethnic groups. In this capacity, it is common for retail agencies to play a dual role, one of organizing a tour by making arrangements with individual tour operators and hotels ect., and another of acting as a vendor of travel services.

Ethnic agents are frequently involved with the transmittal of Prepaid Ticket Advice (PTA) instruments due to their involvement in international air transportation and the process of immigration. The PTA offers the sponsoring relative the opportunity to send an airline ticket to a potential immigrant without incurring the risk of losing the funds spent on the ticket, as refunds are made only to the original purchaser.

The use of PTA instruments by ethnic agents has, at times, been misused in conjunction with immigration. One incident related by an Australian airline executive concerned the Greek community in Sydney, Australia.⁵⁹ Government officials uncovered a scheme whereby Greek agents charged landed immigrants excessive service fees for prepaid tickets, communications and assistance in immigration formalities when bringing their relatives from abroad. This exemplifies how new immigrants must rely upon the honesty of ethnic agents.

⁵⁹Interview with William Noble, Qantas Airways, Vancouver, February 23, 1978.

Due to the need for representation abroad and the lack of a language barrier, ethnic agents can establish reciprocal agreements with travel agents abroad in order to facilitate the transfer of prepaid ticket advice instruments. However, one should not be misled into believing that PTA's have provided a major source of income to ethnic agents. Most agencies rely much more heavily upon income from traffic originating in their own communities. The ability of the ethnic agent to meet the special needs of ethnic community members by communicating in a foreign tongue and providing travel information is a much more poignant reason for the success of the ethnic agency than is income from prepaid ticket advice instruments.

4.2 Ethnic Travel Agent Marketing Strategies

Within the travel industry, ethnic agencies have been noted for their unique marketing approach which relies heavily upon non-conference approved subsidiary agents. Under this approach which is reported to be quite common in the Orient, particularly in Japan and Hong Kong, the principal travel agency uses a sales distribution system comprised of subcontracted agencies and sales personnel which may or may not be approved by airline conferences.⁶⁰

One might hypothesize that the reason for the reliance upon this unauthorized subcontract system of marketing stems from cultural reasons. A casual stroll through Vancouver's Chinatown

⁶⁰Interview with Aaron Lee, AA Travel Industry Inc., Vancouver, February, 1978.

reveals the ominous presence of uniquely ethnic business practice.

Although strictly prohibited by IATA, the "Japanese" approach to marketing travel services is wide spread among ethnic agencies in Canada. This system, incorporating part-time or full-time sales representatives paid on a commission basis contradicts the spirit and rationale underlying travel agent registration legislation previously referred to.

Under the "Japanese approach", ethnic community members benefit from closer and more personalized contacts with their travel agents. The elimination of the grand scale impersonalized approach of the large agencies is made possible by individual agents who have familiarized themselves with a particular facet of the travel industry. Alternatively, ethnic clients may have to rely upon the services of the principal agent if a wider range of services is to be obtained than can be offered by a part-time commissioned agent representative. In accordance with industry legislation in British Columbia, agencies which market air travel services through subcontractors are held liable for the services which they provide. Hence, ethnic travellers who purchase through subcontracted agents benefit from the protection offered by travel agent legislation as well as from personalized attention.

4.3 Co-operation Among Ethnic Travel Agencies

The level of price competition among ethnic agencies is generally agreed to be higher than the level which prevails among non-ethnic agencies. This may be attributed to the smaller

size of ethnic travel firms, the close proximity of ethnic agencies and also to the relatively greater economic impact which foreign travel has upon ethnic community members.

It is probably not incorrect to surmise that following the enactment of travel industry legislation, the level of competition among ethnic agencies diminished. Within a year following British Columbia's registration deadline, four ethnic travel agencies were reported to have ceased doing business.⁶¹ Nevertheless, even with travel agent legislation in effect, controls on discounting among ethnic agents have not been established.

Various ethnic agency groups across Canada including Chinese, Pakistanis and Filipinos, have formed associations in order to encourage the exchange of information among ethnic agents of a similar type and to reach agreements to eliminate ticket price discounting.

An attempt at forming an association of Chinese travel agents in Greater Vancouver was made during the latter part of 1978 by a group of prominent Chinese agencies suffering from alleged revenue losses due to discounting. Approximately 25 agencies in Greater Vancouver have been identified as Chinese travel agencies.⁶² These agencies have been identified in Exhibit 7.

⁶¹Interview with Ivan Cheng, Love and White Travel, Vancouver, July 11, 1978.

⁶²Interview with Ivan Cheng, Love and White Travel Services, Vancouver, July 11, 1978.

Exhibit 7

Chinese Travel Agencies In Greater Vancouver

Corporations

1. AA Travel Industry Corp.
2. Advice Travel Service Ltd.
3. Asian Express Ltd.
4. Continental Travel Agency Ltd.
5. Double Happiness Travel Ltd.
6. Galaxy Travel Agency Ltd.
7. Kowloon Tourist Service International Ltd.
8. Love And White Travel Service Ltd.
9. Mandarin Tours Ltd.
10. Orient Travel Centre Ltd.
11. President Travel Agency Ltd.
12. Quon On Company Ltd.
13. Right On Company Ltd.
14. South East Travel Service (Canada) Co. Ltd.
15. T.P.Y. Travel Service Ltd.
16. Tiki Travel Inc.
17. Wankow Tour And Travel Ltd.

Sole Proprietorships

18. Cathay Travel Service
19. Quon H. Wong. Agencies
20. Spot Travel

Source: Ivan Cheng, Love And White Travel And
Ministry Of Consumer And Corporate Affairs
Lists.

By plotting the location of Chinese agencies⁶³ and comparing their locations with a demographic mapping of persons born in Asia residing within Vancouver, one can readily observe

⁶³Chinese agencies are defined for these purposes as agencies which are involved in the Chinese ethnic travel business and have been invited to join the Association of Chinese Travel Agents.

that Chinese agencies are concentrated in areas with the highest concentrations of Asians as expected. Appendix 3 reveals the location of 23 Chinese travel agencies. There are 15 agency outlets in the Chinatown or Downtown East Side of Vancouver. The bulk of the Chinese agencies are clustered together in this relatively small geographic area.

Just as individuals shop from store to store when purchasing an expensive consumer durable, members of the Chinese community have been known to shop from agency to travel agency for the least expensive price for an airline ticket to the Far East. This practice would be widespread in the travel industry under the net fare remuneration system presented in Chapter 2. The practice is presently a common business practice in major cities in the Orient.

Owners of Chinese travel agencies view discounting as a threat to profitability. For this reason, organizers of the Association of Chinese Travel Agents sought to bring about an agreement to stop discounting and publish a bulletin informing members of correct fares and association activities.⁶⁴ The reason for the inclusion of fare information in the publication stems from the belief that some discounting was the result of incorrect fare information. The organizing of an association of Chinese agencies in Toronto was reported to have eliminated many of the discounting problems among ethnic agencies.

Before considering the effect over time of changes in the

⁶⁴"Oriental Agents Organize to Combat Hanky-Panky", Canadian Travel Courier, Aug. 25, 1977, pp. 1-2.

market structure of ethnic agencies, the issue of whether the formation of associations among ethnic agencies has had a detrimental effect upon the service level provided members of the ethnic community must be addressed.

The characteristics of healthy competition are present within this highly regulated segment of the travel industry. Owners of ethnic agencies benefit from the higher prices charged when a viable agency association enforces IATA and government approved tariff levels. Alternatively, it is clear that the consumer pays more while receiving the same level of services when an agency association is successful in maintaining higher prices.

The advent of consumer protection legislation for the travel industry has increased the barriers to entry for potential travel agents; nevertheless, regulations are not so stringent as to severely restrict entry. Agencies can still establish themselves without an overly long delay. Since the supply of new agents is not limited, agency associations such as ethnic agencies encounter difficulties forming collusive agreements e.g., maintaining authorized price levels.

Although it may seem as if consumers benefit from illegal discounting, the cost in the form of a lower service level must be kept in mind because reduced earnings from commission earnings imply lower profits. In a regulated industry such as the air travel industry, it would seem prudent for the earning levels of travel agents to be available to government regulatory bodies and hence, for discounting of airline ticket prices to be strictly controlled.

4.4 Diversification Of Ethnic Travel Agencies

Within the Canadian mosaic of ethnic groups, one finds a multitude of different ethnic travel agencies specializing to differing degrees in servicing the passenger transportation needs of their respective communities. Immigration patterns in Canada, historians have noted, have followed waves. From the original explorers from France and the British Isles to the recent waves from the Asian subcontinent, immigration from particular areas of the world has tended to be grouped or clustered in the various periods throughout Canadian history.⁶⁵ The longer ethnic minorities have been established in the cities, the greater the probability that members of the group will assimilate and increase the degree to which they interact with the ethnic majority. This sociological phenomenon is reflected in the sales patterns of ethnic travel agencies.

Ethnic travel agents which identify with earlier waves of immigration such as those from Northern Europe tend to be more diversified than are ethnic agencies associated with more recent waves of immigration such as the Chinese and Pakistani ethnic groups. Over the generations, as language differences become less of a barrier, ethnic agencies tend to diversify and diminish their concentration of service to one ethnic group. Similarly, the ethenticity of "new wave" agencies is more visible than it is for "old wave" agencies.

Among individual ethnic agencies, there is a tendency to

⁶⁵Statistics Canada, Canada Handbook-1977, Ottawa: 1977, pp. 34-36

diversify into non-ethnic travel segments of the travel industry. This may include expansion into marketing activities such as cargo marketing, commercial travel and the inclusive tour market as well.

The diversification referred to here is found in the case of AA Travel Industry Corporation, a successful Vancouver-based ethnic travel firm. In January of 1975, Aaron Lee, a member of Vancouver's Chinese community, commenced business selling airline tickets and inclusive tours to members of the ethnic community.

Since its founding in 1975, the firm has expanded rapidly through a diversification programme which has included the development of tours of Western Canada marketed through affiliated agencies in Japan.⁶⁶ Many agencies are of the belief that in order to expand and improve their financial position, they must be successful in marketing to the anglophone community.

As mentioned previously, some ethnic agencies conduct up to 90 percent of their transactions in a foreign language. When AA Travel was first established, sales were conducted almost entirely with members of the Asian community. After three years of operation, the firm's president estimated that in 1977, a full 70 percent of its customers were members of Vancouver's ethnic minorities and that of these approximately 60 percent

⁶⁶AA Travel Industry Incorporated, "Annual Report 1977", (unpublished), Vancouver B.C.

were of Chinese origin.⁶⁷

Ethnic agencies seeking to establish themselves in other segments must, first of all, break through the language barrier and secondly, develop their expertise in another market segment. Travel counsellors at AA Travel have become proficient at providing travel services to clients from Vancouver's downtown business community. Many smaller ethnic agencies have been severely hindered from expanding into other market segments by language and cultural barriers. Typically, these organizations located in the heart of ethnic communities are staffed by new immigrants.

Ethnic travel agents play a role in the distribution of air travel services which is of considerable importance to members of ethnic communities. Due to language and cultural differences, airlines cannot easily provide substitutes for the services offered by ethnic agents. The variety of travel related services provided by ethnic travel agents such as multimodal booking and ticketing as well as other transportation related services reflects the improved service level which the travelling public receives in the distribution system incorporating travel agents as sales intermediaries. From another point of view, the analyst must ask whether the travelling public might not be better served by greater airline emphasis upon internal marketing, considering the 1976 commission expense of \$1.44 billion which faced the world's airlines.⁶⁸

⁶⁷Interview with Aaron Lee, AA Travel Industry Incorporated, Vancouver. Date.

⁶⁸Air Transport World, op. cit., October 1977, p 32.

4.5 Travel Agents Vs. City Ticket Offices

City Sales Offices As Alternative Channels Of Distribution

Airlines have an alternative means of marketing their transportation product. Until the recent growth in the share of airline revenues generated by travel agents, city ticket offices owned and managed by individual carriers generated a much larger share of total passenger revenue. The airlines contend and conference appointment agreements stipulate that the purpose of air carrier reliance upon agencies is to stimulate new traffic, primarily pleasure traffic or to service clients needs in isolated locations.

Differences In Service Characteristics

From the consumer's point of view, the services received from a city sales office differ from those received from a travel agency. Among the most important, is the fact that airline owned city ticket offices emphasize their own transportation services, hence, sales agents may not bring to the traveller's attention all of the options available to him.

Airline operated city sales offices and travel agencies located in urban centres compete for the large and highly stable commercial travel market. One of the service characteristics which travel agents have laid stress on in order to attract commercial customers has been the extension of credit terms to commercial clients. As previously discussed, this additional service or enticement from travel agencies has been viewed as the cause of agency bankruptcies. Airlines maintain their own

commercial accounts and in addition airlines as well as travel agents honour major credit cards.

Carriers have responded to the infringement of the travel agent on the commercial travel market by creating a variety of new services. For example, individuals or firms with appropriate credit ratings may be entitled to "express" ticketing for domestic travel whereby the traveller writes his own ticket. This expedites ticketing procedures greatly and is particularly attractive to commercial travellers who travel frequently.

Another advantage which most city sales offices have in comparison with most travel agencies is the availability of instant information from airline reservations systems. The introduction of the cathode ray tube (CRT) terminal to travel agencies, an important milestone in the evolution of the travel agent shall gradually alter this situation. The implications of the introduction of electronic reservation systems to travel agents are considered in Chapter 5.

The Importance Of Travel Agencies For The City Sales Office

The decision to establish a new city sales office depends upon the marketing strategy of the airline and upon marketing environment characteristics. An Air Canada marketing manager reports that the perceived need of customers, the number of travel agents in the area, the profitability of a region and the demographic characteristics of the area are taken into consideration when deciding to establish a new city sales

office.⁶⁹

The competitive relationship between travel agents and the airlines is also taken into consideration along with other factors in arriving at a decision to establish a new city sales office within a given urban area. The level of service which an airline seeks to provide its passengers in a given area depends upon the number of agents and sales offices in the area. Travel agents, acting through their industry associations may protest the establishment of a new sales office. However, boycotts of airlines by travel agencies because of the establishment of city sales offices have not been an obvious problem due to the limited bargaining strength of travel agencies.

In order to provide better service to commercial travellers, an airline may sometimes adapt its distribution system to the demographic changes of the business community. A recent case in Toronto exemplifies this situation. As more and more firms relocated their offices in the suburbs, and servicing through established Air Canada sales outlets became less and less convenient, higher commission expenses were most likely being incurred among suburban travel agencies. Therefore, the airline reached the decision to establish two new sales offices in the suburbs to better serve the commercial travel market segment.⁷⁰ Although indirectly related to the adversarial relationship between carriers and their agents, this action

⁶⁹Interview with W.A.C. Rowe, Air Canada, General Sales and Service Manager, Vancouver, B.C. March 9, 1978.

⁷⁰Interview with G. Kennedy and D. Tangry, Air Canada, Western Region, Passenger Marketing Division, Vancouver, July 19, 1978.

reflects the belief officially advocated by IATA that travel agents should confine their efforts to servicing discretionary pleasure traffic.

Airlines do not base the decision on whether to establish a new sales office solely on whether internal operating costs are lower than the cost which would be incurred if the services of travel agents were relied upon. It is clear that an airline's city sales office is much more likely to stimulate traffic for the carrier than will supposedly impartial independent travel agencies. Nonetheless, some carriers in the United States have started to deemphasize their reliance upon city sales offices. For example, Braniff Airways which reported that its city ticket offices were costing it approximately 16 percent of airline ticket sales was reported to have dropped its city sales office organization in 1977.⁷¹ Other carriers including Trans World Airlines and Eastern Airlines have followed suit.

⁷¹"Special Report on Airline and Travel Agents", Air Transport World, October, 1977, pp 51-56.

CHAPTER 5 ACCESS TO ELECTRONIC RESERVATIONS SYSTEMS

5.0 The Introduction Of Computer-Based Reservations Systems to Travel Agencies

The focus of this chapter is not so much upon technological developments which are repeatedly being introduced to the industry, but rather upon how various participants in the travel industry stand to benefit from better access to airline reservations systems. Ultimately, an attempt is made at answering the question, "Does the consumer benefit?"

Prior to the introduction of cathode ray tube terminals (CRTs) to travel agents, reservations placed through travel agencies were relayed via telephone. However, as early as 1976, airlines seeking to stimulate traffic experimented with the concept of placing terminals with direct communication to airline electronic reservations systems within wholesale as well as retail travel agencies. The implications of this development for the future of the travel industry are significant and therefore should be taken into consideration in the analysis of the changing role which travel agents play.

Highly sophisticated airline reservations systems with communications links at airline points of service are as essential to the efficient operation of a modern first level air carrier as are the aircraft which transport passengers. Computer-based airline reservations systems perform a variety of vital services in addition to real-time seat availability and inventory. Reservations systems maintain passenger name records

of pertinent information related to the individual passenger.⁷² In addition, present day reservations systems can communicate among themselves and request bookings from other electronic reservations systems. Reservations systems are closely linked with airline ticketing and indeed, computerized ticket printers are presently used by both airlines and agents.

5.1 Airline Competition For Travel Agent Bookings

It is in a carrier's best interest to seek to establish its own electronic reservations terminals (i.e., CRT sets) in travel agents since it facilitates selling the services of the airline which is featured on the system. Even if a variety of carriers inventories are maintained on the system to which the travel agent has immediate access, the agent shall place greater emphasis upon selling the transportation services of the airline featured on the system. For example, on a route served by two carriers, the carrier with more terminals in retail agencies stands to capture the larger market share assuming, of course, that travel agents provide a significant amount of traffic on the route.

The Introduction Of A Reservation System To Travel Agencies

The introduction of Air Canada's Reservec II computer system which includes the inventories of most regional Canadian carriers and a partial inventory of CP Air flights to travel

⁷²United States, Department of Transportation, Office of Facilitation, "Passenger Reservations and Ticketing", Washington D.C., 1971, pp. 2-7.

agents provides evidence of the importance which the placement of CRT sets in travel agencies can have as a marketing tool. Since the Air Canada reservations system is the largest and includes the most services of any electronic reservation system in Canada, (it is anticipated that it shall eventually include all interline partners on a connecting flight basis, car rental firms and hotel accommodations) it has been viewed as the most desirable system to be included in the Canadian travel agent's portfolio of tools, at least from the travel agent's point of view. The electronic reservation system offered by CP Air, the nation's next largest carrier, provides a different variety of airline inventories. Those CP Air flights which overlap with Air Canada flights are included in the Air Canada system, however, agents must make a special request in order to view CP Air flights on their terminals. Air Canada has placed itself in an advantageous position with regard to the placement of airline reservations systems in comparison with CP Air which, to date, has not established remote terminals in travel agencies.⁷³

As of September, 1978, approximately 30 remote CRT terminals had been placed in travel agencies in British Columbia's lower mainland. The agencies chosen by Air Canada to be linked with the airline's electronic reservation system were selected on the basis of how many Air Canada sales they would produce. From a profitability standpoint, individual districts are held accountable for a preestablished return on investment for each

⁷³Interview with Bill Murphy, Pagaesus Systems, CP Air, March, 1978.

terminal.⁷⁴ In the case of the travel agencies which have direct access to Air Canada's system, precautions have been taken to limit the amount of information to which travel agents have access. Agents cannot obtain passenger name lists, instead, they are only provided access to information revealing whether or not space is available on a particular flight. Nonetheless, a wide variety of information including information on individual passengers may be obtained or stored by the travel agent.

Electronic Reservations Systems in U. S. Travel Agencies

Airline competition for travel agent ticketing in the United States has been much more competitive than it has been in Canada. This can be attributed to the large number of trunk carriers with extensive electronic reservations systems. The essential difference between computerization developments in Canada vis-a-vis those in the U.S. is the greater degree of choice which American agents have because of the greater number of systems available.

Due to United States Justice Department disapproval of the joint development of an airline/travel agent reservations system, United Airlines, American Airlines and Trans World Airlines have each decided to market their systems to travel agents on a separate basis. Both United's and American's systems are designed for their own ticket agents and hence, their own flights are displayed first on the CRT.⁷⁵ The significance of

⁷⁴Interview with W.A.C. Rowe, Air Canada, General Sales and Services Manager, Vancouver, March 9, 1978.

establishing an effective travel agent reservations interface with airline reservations systems is made evident by the fact that in United's case, some 50 percent of the carrier's passenger revenues were generated by travel agents in 1976.⁷⁶

Each carrier appears to utilize its own criteria for the selection of agents chosen for installation of terminals. United Airlines for example, has established minimum revenue levels which agencies must fulfill in order to qualify for the installation of a CRT terminal. An approved agency must either generate \$300,000 in annual airline revenue with United or an annual air revenue of \$1 million of which 15 percent must be on United.

Marketing Advantages Through Automation

The automated ticket printer which is used in conjunction with reservations terminals by travel agents and commercial accounts has become a reality for many large Canadian travel agencies. Such ticketing accessories were introduced previously to travel agencies in the United States. Printers facilitate the writing of most domestic and some international airline tickets as well as the payment of net revenues to the carriers involved.

Travel agencies which specialize in selling domestic airline transportation products to commercial travellers are the primary users of the ticket printer although this is far from the only group which benefits from their use. Consequently,

⁷⁵"Airlines Spar Over Ticketing", Aviation Week and Space Technology, February 2, 1976. p. 30.

⁷⁶ Op. Cit., Air Transport World, October, 1977, p. 33.

travel agent associations have opposed efforts by Air Canada to provide commercial customers with terminals and ticket printers free of charge which detracts from the sales of travel agencies, particularly from travel agencies specializing in commercial travel.⁷⁷ Agents fear the next step by Air Canada may be to offer commercial accounts a commission on their purchases of airline tickets. The adversarial relationship between airline and travel agent is apparent once again in the minor conflict which might be fundamentally viewed as an attempt on the part of airlines to minimize commission expenses and on the part of travel agents to maximize commission earnings.

5.2 Benefits And Costs Of System Installation for The Travel Agent

For those agencies which are fortunate enough to meet the criteria established by the airlines to obtain a cathode ray tube terminal, a variety of marketing and operating efficiency benefits are forthcoming. Two managers of Vancouver-based travel agencies which have been operating with Air Canada remote terminals and ticket printers for six months reported the following benefits:⁷⁸ Reservec II provides travel consultants with quick access to reliable information; reservations can be changed or altered in a much more convenient manner than under previous methods; and a great deal of information previously

⁷⁷"Commercial Accounts to Get Ticket Printers", Canadian Travel Courier, June 16, 1977, p. 1.

⁷⁸Interview with Malcolm Nicholson, P. Lawson's Travel, Vancouver, March 30, 1978 and Gordon Rees, Bayshore Travel, Vancouver, April 6, 1978.

only available from manuals becomes available through the airline electronic reservations system.

Agencies using the high speed communications links provided by real-time access to computer-based reservations systems benefit from fewer minutes spent on the telephone and/or better utilization of existing communications resources. On the other hand, the cost of data communications links must be borne by the travel agent according to Air Traffic Conference or IATA regulations.⁷⁹

In addition to lower communications charges, users of CRT terminals report fewer telephone calls returned to customers. A substantial time savings occurs because travel agents are able to confirm passenger reservations while the customer waits. This elimination of most "call-backs" by the use of a real-time system is an important benefit which makes CRT sets particularly attractive to understaffed travel agencies.

Due to the relatively low commission rate on domestic travel (approximately 7.5 percent), agents incur losses when providing services for short-range domestic journeys.⁸⁰ The efficiency provided by airline reservations systems terminals makes it possible for travel agents to cover fixed and variable costs associated with low margin sales such as domestic airline sales.

⁷⁹"Automated Services Provided to Travel Agents Located in the United States", Air Traffic Conference of America, Passenger Committee Bulletin No. 19, Washington D.C., March 31, 1978.

⁸⁰Touche Ross and Company, Joint Travel Agent/Airline Economic and Value Study, reported in "Travel Agents Lose \$23 Million on Domestic Sales", Airline Executive, July, 1978, p. 40.

The presence of an airline's reservation terminal within a travel agency provides a certain degree of promotional benefit. Commercial customers may be attracted to travel agencies which appear to be progressive. A reservation terminal projects the image of fast and efficient services. Moreover, travel agency employees may enjoy the challenge of operating the CRT terminal and learning the many subprogrammes associated with it. Furthermore, it is clear that the "professional" or "airline" image is fostered by the presence of a CRT set in a travel agency.

The benefits which the travel agent derives from the introduction of an airline reservations system are not without costs to agents, competing carriers and possibly even to the consumer of air travel services.

Airlines have agreed through conference regulations to charge travel agencies or travel wholesalers a monthly fee for the use of CRT terminals and automatic ticket printers. The major training cost is the opportunity cost of the time which agents must devote to learning to use CRT devices. Assuming that agents earn an average commission of 8.5 percent, it would be necessary for the agent deciding whether to add an extra terminal to sell an additional \$3,117 of tickets each month in order to cover the monthly fee.⁸¹

Using average fare per ticket information as calculated in

⁸¹Op. Cit., Interview with Malcolm Nicholson, March 30, 1978. In Air Canada's case an initial installation fee of \$100 is charged followed by subsequent monthly payments of \$265.

the 1978 Touche Ross study of travel agent profitability, an agent would have to sell 20.9 domestic point-to-point tickets or 4.9 international tickets at the normal fare in order to cover the cost of one CRT terminal. One should bear in mind that this analysis considers U.S. travel agent commissions which are generally higher than Canadian commissions due to the open rate situation prevailing in the United States.

One of the primary dangers of the Canadian travel agent industry's reliance upon a single airline reservations system which gives preferential display of one carrier is the possibility of increasing airline industry concentration. Travel agents may gradually become dependent not only on the flight display of one carrier but also upon other services offered by airline management information systems including marketing and accounting systems. With regard to the latter, independent firms have developed which provide travel agencies with management information services.

Computer inter-face firms have the potential of lessening the dependence of the travel agent on a single carrier as well as providing travel agents with access to airline as well as tour operator reservations systems.

From the travel agency as a small business point of view, it is advantageous to obtain real-time access to airline reservations systems provided that the level of traffic serviced by the agent is sufficiently high.

5.3 Benefits And Costs Of System Installation For The Airlines

In Canada, Air Canada stands to benefit substantially by

placing its CRT terminals in travel agencies since its market share shall undoubtedly increase, *ceteris paribus*. Another significant benefit accruing to the carrier providing the system is derived from the dissemination of current fare and other marketing information to travel agents hooked into the system. Carriers can better dominate their sales intermediaries if they are the primary source of marketing information for the sales intermediary.

Carriers with a substantial portion of their sales through travel agents may lose a part of their market share to aggressive airlines with an effective programme of placing CRT terminals in agencies. This issue is particularly pertinent in the United States where many carriers compete for the right to place terminals in travel agencies. Although impractical, the possibility of placing more than one CRT terminal in larger agencies should not be ruled out.

Airlines which couple the placement of terminals with the placement of airline ticket stock can also benefit from a substantial short-term cash flow. For example, Trans World Airlines would benefit from the issuance of a ticket for another airline if the ticket were issued on TWA ticket stock. The reason for this is that cash flows first to the host carrier then to the conference clearing house for distribution. This benefit provides additional incentives to carriers to provide agents with individual airline ticket printers.

Whether installation and monthly rental fees cover the cost which the airline incurs implementing electronic reservation systems to travel agents is not entirely obvious from the

limited amount of cost information available to the public. Nevertheless, the fact that special Air Traffic Conference regulations had to be adopted to inhibit carriers from entering into a price war over CRT terminal placement coupled with Air Canada's move to offer complementary CRT terminals and ticket printers to commercial accounts tends to indicate that the benefits for the carrier of additional traffic generated outweighs the cost of establishing and maintaining peripheral terminals.

5.4 The Benefits And Costs Of System Implementation for The Consumer

The benefits which consumers of travel services receive from travel agents with electronic reservations systems are difficult to measure. On certain occasions, such as when airline telephone reservation lines are busy, the advantage of the CRT becomes quite apparent. Other advantages such as those associated with improved accuracy are less obvious. The major benefit cited by most agents who have recently had CRT sets introduced to them is the ability to service customers more rapidly.

As previously outlined, travel agents pay a monthly rental fee for the right to operate remote video terminals. It is not entirely clear that airlines recoup the entire cost of remote terminals in the form of user fees. The cost to the airlines of establishing additional terminals including hardware, software, and communications links is not insignificant. For example, United Airlines was reported to be prepared to spend \$700 million on agent terminals in 1976.

Given the regulated nature of the industry and the fact that the cost of improvements in customer service levels can ultimately be felt by the consumer, the chain of cost impacts may follow a sequence wherein travel agents initially demand higher commissions, citing larger losses on ticket sales. Once airline conferences are cajoled into augmenting commission levels, the carriers in turn follow by requesting higher fare levels from regulatory bodies. The increases in cost which remote travel agent terminals contribute to overall airline cost increases may not be very great relative to other rapidly rising costs such as commission costs, nonetheless, they are a contributing factor which should not be ignored.

5.5 Long-term Implications

The introduction of electronic reservations systems to travel agents in Canada by the national carrier, Air Canada, has important implications for the structure of the airline and travel agent industries and consequently for the level of service which consumers receive.

Air Canada presently has the largest share of the transcontinental Canadian market with CP Air trailing far behind. A monopoly in the placement of reservations terminals in travel agencies by Air Canada at least during this introductory stage can easily result in a greater concentration of power with one semi-autonomous, government-owned carrier. One might question the belief that greater concentration within the airline industry is in the consumer's best interest.

From the consumer's point of view, a computer interface

system providing travel agents with access to the reservations systems of all carriers serving Canadian points would offer a wider range of reservations services while at the same time, eliminate the preferential treatment offered by single airline reservations systems.

On another industry level, that of the travel agent industry, the introduction of electronic reservation system terminals may result in future structural changes especially in that segment of the industry specializing in the commercial travel market. One can attribute this to the minimum financial requirements which have been established by the airlines in marketing their reservations terminals to travel agents. The effect of the requirements is that only the larger, more prosperous agencies are in a position to obtain reservations systems; hence, the trend toward industry concentration to the detriment of the consumer is the implied result. Concentration in the United States travel agent industry since 1970 has been noticed in the C.A.B. investigation of commission levels.⁸²

One might argue that as the travel agent industry becomes more capital intensive, the industry, which is presently composed of many independent small business and few large firms, shall move toward greater concentration. Similarly, if economies of scale can only be taken advantage of by larger firms, then it follows that consumers stand to benefit from the improved service levels offered by larger firms with CRT terminals.

⁸²Op. Cit., United States, Civil Aeronautics Board, "IATA Agreements Concerning Agency Matters--Uniform Commission Rates", pp. 80-107.

Although the electronic reservations introduction phase stands to alter the composition of the travel agent industry, some segments of the travel industry shall probably not be affected significantly. For example, ethnic agencies are protected by the unique services which they offer. Similarly, northern travel agencies which are unlikely to tie into airline reservations systems will most likely retain the same level of business because of the protection offered by their geographic monopolies.

In summary, airlines which succeed in obtaining a preferential position in providing flight information and other services to travel agencies shall benefit from the capturing of a larger market share. Larger agencies in the commercial travel market which have the financial resources available to them to provide their customers with the speed, accuracy and convenience of real-time access to electronic reservations systems shall probably benefit to the detriment of the agencies servicing the commercial market without electronic reservations terminals.

CHAPTER 6 EVALUATION OF TRAVEL AGENT REMUNERATION ALTERNATIVES

6.0 Method Of Evaluation

Description of the benefits and costs which air travellers and air carriers receive from the services performed by the travel agent has been presented in order to reveal the essential role which the travel agent plays in the marketing of travel services to the travelling public. Desirable service attributes of air transportation marketing systems have been referred to in discussions of current issues facing the travel agent industry.

The purpose of this chapter is to evaluate commission and non-commission alternatives, and select the "best" alternative. In order to do so, criteria for evaluation and public policy objectives must be defined and clarified. After the most attractive alternative has been selected, it is then recommended for adoption and implementation by the Canadian Transport Commission. It is also possible that an airline conference, either international or domestic, would be willing to implement a remuneration alternative which it deemed to be in its favour.

6.1 Service Attributes

Many desirable service characteristics associated with an efficient passenger transport marketing system have arisen in the preceding chapters. The service attributes which have been

identified for the purpose of policy analysis include the following:

- a) impartiality vis-a-vis carrier and mode of transport choice
- b) individual attention
- c) ability to provide travel services to specialized market segments
- d) rapid access to passenger reservations information

It is generally agreed that the impartiality of the sales intermediary is a desirable characteristic since the client is presented with a greater number of alternatives to choose from. Impartiality can extend to the choice between modes as well as the choice between carriers.

Another service attribute which has been associated with the travel agent industry is personalized attention. It has been argued by proponents of small businesses that individual attention and knowledge of an individual's comprehensive travel needs cannot be adequately provided by larger airline operated city sales offices.

The ability of the passenger transportation marketing system to serve a diverse set of market segments such as travellers from the business community, holiday travellers and ethnic community travellers is a service characteristic taken for granted under the present system. As outlined in Chapter 4, some travel agencies have specialized in individual market segments because of their ability to meet the demand for unique services. A travel agent remuneration policy would not eliminate the ability of the marketing system to meet these specialized

needs. At the same time, it should minimize the cross-subsidization of specialized clients by clients not requiring specialized assistance.

Reservation systems and access to them have come to be important determinants of the level of customer service which air carriers and sales intermediaires provide their clients. As described in Chapter 5, rapid or "real-time" access to airline reservations systems is a highly desirable characteristic associated with the air travel industry. It is likely that different remuneration alternatives will foster the development of electronic reservation systems in travel agencies to a different extent. Therefore, this attribute should not be excluded from consideration in the analysis.

It is difficult to judge the relative importance of each of these attributes however, it does not appear to be far from the truth, considering descriptions of the industry, to state that impartiality and the ability to provide personalized attention are among the most important.

6.2 Criteria For Evaluation

As part of the policy analysis procedure, each alternative is analyzed in relation to public policy objectives designed to reflect the long-run best interest of the public. Objectives which will be considered in the decision include the following:

1. Service Level Objectives

- impartiality
- access to reservation information
- personalized attention
- service to market segments

2. Economic Objectives

- user pay
- economic efficiency

3. Political Objectives

- user pay
- avoid cross subsidization between user groups

4. Regional Development Objectives

- adequate service levels to small communities

The desirable service characteristics which have been apparent under the status quo such as impartiality with regard to carrier choice and individual attention may be considered to comprise the service level objectives.

The economic objectives considered include the implementation of the user pay philosophy and the avoidance of subsidies flowing from the general public to the owners of travel agencies. The general rule here is that commission levels should not be so high that regulatory agencies grant airfare increases. With respect to economic objectives, alternatives should be selected on the basis of whether the ratio of service level to commission expense is increased i.e., on the basis of improving economic efficiency.

In a regulated industry such as the air transport industry, lack of managerial control of marketing variables including the ability to set prices and to decide where services should be provided implies that regulatory involvement may be necessary to

ensure that economic efficiency objectives related to the air transport marketing system are not neglected. Specifically, the trade-off between the level of marketing services provided by travel agents and air carriers must be juxtaposed against the opportunity cost of devoting resources to marketing instead of other services. Evidence of rapidly rising commission expenses and travel agent profit levels presented in Chapter 2 serve as indications of economic inefficiencies, given the state of the industry.

Political objectives related to the decision to choose an alternative remuneration policy must be in line with federal political objectives concerning travel and transportation in general. The magnitude of the remuneration issue must be realized. Of the importance of the issue within the travel agent industry there is no question, however, on a federal political level, it is not very significant. Hence, because the impact for political purposes is insignificant, one can expect that regulatory decisions made by the Canadian Transport Commission will reflect the economic objective of implementing the user pay philosophy.

Regional development objectives referred to are oriented toward reducing regional economic disparities and ensuring that adequate air transport marketing services are provided to residents of isolated communities. In the interest of northern development, it would seem prudent to provide monetary incentives to entrepreneurs to provide better service to residents of isolated communities as far as is practicable.

6.3 Evaluation Of Alternatives

The Net Fare Remuneration Alternative

The adoption of a net fare concept would bring about drastic long-run changes in the travel agent industry and in the way in which air transport services are marketed by the airlines. With agencies no longer receiving commissions, the optimal firm size for many market segments would increase because revenues would decrease from their present levels and many small firms would be hard pressed to cover fixed costs. The result would be the increase in the concentration of larger firms and possibly the institution of franchise agreements in an attempt to cover fixed costs.

Counteracting this effect is the lack of clear substitutes for the personal travel consulting attention provided by small travel agencies. In other words, some clients would still be willing to pay an additional service fee for the personalized travel consulting offered by travel agents. These people would probably be few in number.

Service Level Objectives

With net fares, the impartiality of the agent with regard to carrier choice would be retained to the extent that the same fare could be charged for the same carriers on the same route. On the other hand, travel agents would become increasingly biased toward the choice of other modes of transportation which retained the commission form of remuneration. However, as previously pointed out, inter-modal competition in long distance

passenger transportation is not a major factor in many markets.

Assuming that net fares would result in increased concentration and lower profit levels, one could expect few agencies would be able to afford the additional cost of introducing an electronic reservation system. Direct access to airline electronic reservation systems would probably be enhanced by the air carriers themselves because additional internal channels of distribution (equipped with CRT sets) would be established in order to replace the reduced service level provided by travel agencies. However, the increased concentration in the industry caused by the adoption of a net fare remuneration approach could result in an increase in the likelihood that larger agencies would be financially capable of adopting electronic reservation systems.

With regard to the ability to provide clients with individual attention under this alternative, the demise of the small agency would serve to support the argument that the ability to provide personalized attention would be reduced. Although a trend in this direction would result, individualized travel counselling attention could be provided in a similar manner by small branch outlets of larger firms which would be able to survive by spreading fixed costs over many branch outlets.

Service levels to some market segments would be adversely affected by the adoption of net fares. Alternatively, in market segments where travel agents provide services which are not readily provided by the carriers, such as in the case of the ethnic market segments, clients would be willing to pay for

specialized services. With regard to the commercial travel market segment, one could expect greater emphasis on sales through airline city sales offices because many commercial travellers would be unwilling to pay extra for the services offered by the travel agent. (This would also be true for non-commercial travellers).

Economic Objectives

The institution of a net fare travel agent remuneration procedure would eliminate any subsidization of the travel agent industry by the carriers which existed under the fixed remuneration scheme. This is because fees charged by travel agents would be established in the marketplace. In this regard the net fare alternative is in line with the user pay philosophy.

On the other hand, if airlines were forced, on an individual basis to emphasize internal marketing channels. Hence incurring greater marketing costs and in turn passing these increased costs on to consumers in the form of higher fares, then this alternative would not be in the travelling public's best interest as a misallocation of resources would result. It is generally agreed that commission expenses would be less under the net fare alternative than they would be under an open rate situation as discussed in Chapter 2.

Political Objectives

It goes without saying that owners of travel agencies would object to the removal of the protective fixed commission

blanket which has fostered the development of an extensive industry. However, in the long-run, the elimination of outright commissions by regulatory support of the net fare concept should result in lower airfares, ceteris paribus. Clearly, this reflects the user pay philosophy is in the public's best interest. Moreover, travellers would still have the opportunity to pay for travel counselling services if they so desired.

Regional Development Objectives

Under the net fare concept, small agencies in small communities would be faced with serious decreases in revenues due to the shift in market share to the airlines in areas where travellers could conveniently purchase their tickets directly from the carriers, such as at airport ticket counters. In areas where agency competition is limited, clients could expect to pay monopoly prices for travel agent services unless restrictions were imposed.

The Uniform Commission Alternative

This is the remuneration alternative with which participants in the industry are most familiar. As discussed in Chapter 2, uniform commission structures prevailing until 1975 differed only with regard to domestic or international travel. The uniform commission alternative considered here would not make such a distinction because the nature of the international and domestic air travel markets have changed dramatically in the last five years.

One should note that the level of commissions has an

important impact upon the structure of the industry. Uniform, but low, commissions would not encourage the formation of small agencies.

Service Characteristics

The rationale underlying the long-standing defense of uniform commissions by air conferences is based on the premise that uniform commissions foster the impartial choice of carriers by agents. This is one of the strongest arguments in favour of the retention of this remuneration alternative since airline owned and operated city sales offices are unlikely to provide clients with a truly unbiased choice of carriers with differential commissions prevailing.

The level of uniform commissions determines whether agents will be induced to introduce electronic reservation systems to their firms. Under a uniform commission structure which is sufficiently high, small agencies flourish because there is no special incentive to distribute fixed costs as under the net fare alternative. The emphasis upon marketing air travel services through travel agents encourages the placement of electronic reservation systems in travel agencies and hence, encourages a higher customer service level.

The uniform commission alternative promotes the development of a personalized travel consulting relationship between client and agent because such relationships are more easily provided by smaller firms. Furthermore, clients are more likely to place their confidence in the travel agent's choice of carrier when the financial incentive to select the carrier offering the

highest commission is present.

Difficult to service market segments such as the ethnic market segments will be served to some degree whether uniform commissions are offered or not. Nonetheless, uniform commissions will tend to favour those market segments which are the least costly to service. Under a commission alternative which offers agents the same rate for servicing the commercial travel market segment, (a market segment relying heavily upon domestic transportation services), as it does for servicing the ethnic market, (a market segment heavily involved in international travel), marketing service levels will be relatively higher for the former than for the latter.

Economic Objectives

By retaining uniform commissions, cross subsidization of one market segment by another is retained. This is because remuneration levels established through the airline conferences and the government regulatory framework reflect average costs, not the cost of providing services to individual market segments. Users of specialized travel agent services do not bear the full cost of the marketing services which they consume. However, because uniform commissions are necessarily agreed upon, and the conferences are instrumental in setting commission levels, it is unlikely that the level of commission expenses will be so high that regulatory agencies are requested to increase fares.

An associated economic factor related to the uniform commission alternative is the reduction of business risk

resulting from stable and predictable remuneration levels.

Political Objectives

Uniform commissions are popular among travel agents relative to the net fare alternative which would have a dramatic impact upon the industry. Aside from the difference between international and domestic commission levels, uniform commissions represent the status quo in Canada. From a public policy point of view, uniform commissions represent a compromise between the marketplace generated travel consulting fees under the net fare concept and the exorbitant commission expenses under a policy of deregulated incentive commissions. Nevertheless, uniform commissions do not reflect the costs incurred by travel agents in providing marketing services.

Regional Development Objectives

As discussed in Chapter 2, uniform commissions do not reflect the higher cost of providing air travel marketing services to residents of remote communities in Canada. Nevertheless, given a sufficiently high level, they do provide enough incentive for agencies to prosper, while at the same time they provide consumers with an inherent form of protection against monopolistic service fees which could arise under the net fare alternative. Regional development objectives might best be achieved by providing additional financial incentives to travel agents in smaller communities. This possibility is addressed in the next alternative to be considered.

The Incentive Commission Alternatives

For purposes of analysis, two types of incentive commission alternatives are considered: First, the incentive commissions which develop under an unregulated situation are evaluated against the stated objectives. Second, regulated incentive commissions are considered. The latter could be regulated in such a manner that regional development objectives could be attained.

The Unregulated Incentive Commission Alternative

It is possible for incentive commissions to exist as a method of compensating travel agents for the services which they provide under both regulated and deregulated conditions. It has been shown by the open rate situation prevailing for international air travel marketed by travel agents in the United States that incentive commissions are a natural economic phenomenon which develops in an unregulated environment to the benefit of the carrier implementing the commission structure.

Commission schedules based upon either volume or destination incentives are termed incentive commission structures. Examples in Appendix 1 reveal that such commissions are oriented toward the stimulation of group travel and travel on particular routes. What is not evident from this appendix is that carriers use incentive commissions to increase their sales levels through larger travel agencies which are capable of qualifying for volume incentives.

It has been argued that incentive commissions have been the major cause of spiralling commissions in the United States. They

have also been attributed to have caused a shift in power to the volume specialists and hence, have contributed to concentration within the industry. In the extreme case, firms may become, for all practical purposes, agents of the firm offering the most attractive incentive scheme.

Service Objectives

Incentive commissions alter the travel agents unbiased attitude toward selling the services of individual carriers. Carriers invariably offer different levels and types of incentives which entice agents to emphasize the air transport services of the carrier with the most attractive financial incentive. However, the introduction of incentive or "open" commissions would not completely destroy the unbiasedness of the agent. Consumer loyalty would diminish for those agencies which are highly biased in their choice of carrier. This would result from the fact that air travellers would realize that they were not being informed of all of the alternatives available in the market, i.e., suboptimal booking would result.

Similarly, impartiality with regard to inter-modal choice could be affected by an unregulated incentive commission situation which resulted in very high levels of remuneration. This is true of both the uniform and the net fare alternatives because they are capable of providing travel agents with either low earning levels (as may be the case with net fares) or high earning levels (as may be the case with uniform commissions). Nevertheless, an unregulated incentive commission structure is more likely to result in higher overall remuneration levels for

agents.

The tendency toward concentration resulting from the introduction of incentive commissions would speed up the process of introducing electronic reservation systems, to volume-specialists, many of whom already have CRT terminals. Small firms adversely affected by incentive commissions because they are not large enough to qualify for large incentives would be hindered from obtaining real-time access to electronic reservation systems. The overall level of earnings is important here. If incentive commissions offer small firms earning levels which are greater than what would be achieved under other alternatives, it is conceivable that small travel agencies would be more likely to have the financial resources available to introduce electronic reservation systems.

The high commission expenses attributed to an open commission structure would make it economically feasible for carriers to open new city sales offices especially in locations with high airline passenger sales where sales could be diverted from existing agencies. This possibility combined with the fact that incentive commissions favour larger firms, tends to indicate that clients would receive a lower level of personalized attention.

Earning levels of agencies involved in specialized markets such as the ethnic markets could be adversely affected by incentive commissions as agencies involved in specialized market segments such as this are typically smaller firms. Other market segments such as the commercial travel segment could, alternatively, benefit from a higher level of service. However,

unregulated incentive commissions would not be designed to meet the needs of specialized market segments. Travellers requiring specialized travel agent services would probably receive a lower level of service under this alternative because agencies specializing in smaller market segments could not take full advantage of incentives offered.

Economic Objectives

Unregulated incentive commissions result in higher commission expenses for the carrier which may eventually be shifted to consumers in the form of higher airfares. To the extent that higher commission expenses are reflected in higher airfares, the economic objective defined as implementing the user pay philosophy is further achieved. Moreover, incentive commission structures are congruent with economic objectives in that structures are generally designed so that different air transport marketing costs for different services are reflected in the commissions offered agents.

On the other hand, with airfares closely regulated by the C.T.C., unregulated commissions result in disproportionately large earning levels for agencies as was revealed in the discussion of international commission levels in the United States. The inability of airline conferences to control commission levels and the reluctance of regulatory bodies to allow concomitant increases in airfares may be cited as a cause of the misallocation of resources between airlines and travel agents. Although high levels of service would be provided to most market segments, the cost in the form of airline commission

expense would be excessively high.

Political Objectives

The higher earning levels offered by unregulated commission structures would be popular among owners of travel agencies. However, from a public policy point of view, travel agent remuneration levels could justly be called exorbitant if commissions were deregulated while airfares remained under strict regulatory control. In the long-run, passengers would be receiving a lower level of service than that which they could be receiving if either airfares and commissions were deregulated or alternatively, both were regulated. In other words, unregulated incentive commissions do not clearly reflect the user pay philosophy.

Regional Development Objectives

Isolated communities would most likely not receive any special attention under an unregulated incentive commission scheme. This is due to the fact that carriers concentrate their marketing efforts in the most profitable market segments. These are typically large urban markets. Small firms would most likely not be able to qualify for volume incentives because sufficiently high traffic levels could not be generated.

The Regulated Incentive Commission Alternative

This alternative represents a tempering of the extremes presented by unregulated incentive commissions. Commissions could be designed in such a manner that the attainment of

objectives could be better achieved. As revealed in Exhibit 8, the regulated version of the alternative achieves the objectives to a greater extent on all counts than does the unregulated commission incentive scheme.

Service Level Objectives

The loss of impartiality of the travel agent would be reduced by the regulatory process which requires agents to file commissions with the C.T.C.

The acceptance of incentive schemes which would not neglect the interests of small agencies would indirectly improve consumer access to electronic reservation systems. Similarly, the promotion of small agencies would be more likely to provide travellers with individual attention and service in specialized markets.

Economic Objectives

Regulatory control over incentive commission structures allows public policy makers to set commission levels to reflect the user pay philosophy. Moreover, the economic efficiency of the system can be regulated by restricting exorbitant remuneration levels.

Political Objectives

By regulating incentive schemes so that they support small businesses, the regulated incentive commission alternative becomes more popular. However, clients requiring special services from specialty travel agencies are unlikely to bear the

full cost of the services provided by them. To this extent, cross subsidization of one market segment by another is present.

Regional Economic Objectives

In this regard, regulated incentive commissions are superior. The higher cost of providing marketing services to travellers can be incorporated in incentive commissions which small travel agents in smaller communities receive. The impact upon overall airline marketing costs of this alternative would not be great for most carriers.

Summary Of Objective Achievement

For the purpose of presenting a visual display of the preceding evaluation of remuneration alternatives, a summary matrix is presented in Exhibit 8. This is not meant to be a substitute for the preceding text and caution should be exercised in interpreting the author's summarizations of the degree to which individual alternatives have been achieved. This table should be interpreted with care as it neglects to reveal the relative importance of each objective.

6.4 Conclusion

Each of the remuneration alternatives considered in this analysis has its own advantages and disadvantages in relationship to the objectives which have been specified. Essentially, what the analyst must do is select the alternative which best fulfills these objectives. In order to do this, subjective judgement concerning the relative importance of the

various objectives necessarily comes into play.

In the author's opinion, economic and service level objectives are the most important objectives. The user pay philosophy and regional development objectives conflict in that attempts to subsidize one group of users may impose additional costs upon another group. The achievement of political objectives is very important in the selection of an alternative, indeed, government agencies can not be expected to support the introduction of a policy change which opposes political goals. Nevertheless, compromises are frequently made.

The alternative which is recommended for adoption by the Canadian Transport Commission to serve as the commission structure for Canadian travel agents for both domestic and international travel is the regulated incentive commission alternative. This alternative is not the "best" alternative on all counts; instead, it serves as a compromise. Through the process of arbitration, carriers and governments would be able to arrive at incentive commission structures which would reflect the interests of the travelling public as well as the carriers. For example, the same volume incentives for particular destinations could be authorized for a number of carriers in order to ensure that impartiality with regard to carrier was retained. Similarly, in the interest of attaining economic objectives, higher commission levels could be authorized for the marketing of tours through travel agencies.

Exhibit 8

Summary Of Remuneration Scheme Objective Achievement

Objectives	Remuneration Alternatives			
	Net Fare	Unif. Com. ¹	Reg. Inc. Ccm. ²	Unreg. Inc. Com. ³
Service Objectives				
a) impartiality	fair	v.g.	poor	v.p.
B) info. sys. acc. ⁴	fair	good	good	fair
c) individ. attn. ⁵	poor	fair	fair	poor
d) service to spec. mkts. ⁶	good	fair	poor	v.p.
Economic Objectives	v.g.	poor	good	poor
Political Objectives	v.g.	poor	good	poor
Regional Development	poor	poor	v.g.	v.p.

"v.g." means very good.

"v.p." means very poor.

¹"Unif. Comm." is the uniform commission alternative.

²"Reg. Inc. Com." means the regulated incentive commission alternative.

³"Unreg. Inc. Com." refers to the unregulated incentive commission alternative.

⁴"info. sys. acc." means access to airline electronic reservation systems.

⁵"individ. attn." refers to the ability of the travel agent to provide individual attention.

⁶"service to spec. mkts." is the ability of the system to provide services to air travel market segments.

Services to specialized market segments such as those in urban ethnic and isolated northern communities which were identified by the C.T.C. as important, could be retained by allowing greater remuneration incentives in these market segments.

Given the fact that airfares are regulated by the federal government and in most provinces, entrance into the travel agent industry is provincially regulated, it follows that travel agent remunerations should be regulated as well. Moreover, it has been shown that regulated incentive commissions can be adjusted by regulatory bodies so that consumers receive an adequate service level, airlines are not excessively burdened with commission expenses and travel agents are induced by a sufficiently high remuneration level to provide air travel services to the travelling public which are necessary for an efficient air transport industry.

CHAPTER 7 SUMMARY

7.0 Summary

The environmental changes in the past decade associated with the airline industry have brought about tremendous changes in the role which the travel agent plays in the airline industry. In the mid-1970's, the relationship between airlines and their agents began to deteriorate as the result of rising commissions. Faced with higher commission expenses, carriers caused government agencies to question whether travel agent services provided to the public were at a sufficient level to warrant such an expense. More fundamentally, the role of the travel agent in the airline industry was brought into question.

In Chapter 1, the ways in which air travellers, owners of travel agencies, and air carriers benefit from the services provided by travel agents was presented. The various travel services provided by agents including airline ticketing, the organization of tours and the fulfillment of passenger reservations requirements were described in subsequent chapters.

The specific objective of this thesis has been to select a travel agent remuneration policy for use in Canada, which would provide air travellers with an adequate level of service, while at the same time avoiding excessive commission expenses which are economically inefficient and wasteful. Subsequent to the evaluation of the four remuneration alternatives, net fare,

uniform commission, unregulated incentive commissions and regulated incentive commission, the conclusion was drawn that a regulated incentive scheme would "best" meet the objectives specified and hence be in the public's best interest.

The objectives specified which included service, economic, political and regional development objectives were chosen because they were felt to best reflect the interests of the public with regard to the provision of air travel marketing services either directly by the carrier or through travel agents.

With the introduction of regulated incentive commissions which would offer Canadian travel agents incremental commissions depending upon traffic volumes generated to specific destinations, the spiralling commission expenses which have been experienced in the United States in recent years would be avoided. Furthermore, government policy makers would be in a position to regulate commission levels in such a manner that the user pay philosophy with regard to the purchasing of air travel marketing services could be further implemented. The initial impact of the incentive commission alternative would be moderate in the sense that the structure of the industry would not immediately be altered. Eventually, policy makers could use their regulatory power to stimulate the provision of services to particular market segments deemed to be in need. For example, the Canadian Transport Commission might seek to stimulate the growth of smaller firms.

Aside from addressing the major policy issue of selecting an appropriate remuneration scheme, background information

directly and indirectly related to the thesis topic has been presented.

The travel agent industry is regulated by provincial travel industry legislation which seeks to protect consumers from the risk of tour wholesaler or retail travel agent bankruptcy. Airline conference entrance requirements are an insufficient means of providing consumers with protection against financial injury. The enactment of legislation requiring mandatory contributions to compensation funds has been praised as a more comprehensive approach to protecting the travelling public.

An important characteristic associated with the travel agent industry is the ability to provide specialized services to market segments not readily served directly by the airlines. Two market segments which exemplify this ability include the ethnic and commercial travel market segments. Air carrier management is faced with the decision of whether to emphasize sales externally, through the travel agent channel of distribution or internally through city sales offices.

The use of remote electronic reservation system terminals in travel agencies emphasizes the importance which access to accurate, up-to-date reservation information plays for travel agents in many market segments. The impartiality of the travel agent with regard to carrier choice is threatened by the biasedness of reservations systems owned by individual carriers.

Discussion of changes in the travel agent industry environment has been instrumental in the evaluation of alternative travel agent remuneration schemes. Although models have been used in forecasting the impact of various remuneration

alternatives, whether the implementation of a regulated incentive commission policy by the Canadian Transport Commission for Canadian agents selling international and domestic air travel service is in the public's best interest can, in fact, only be revealed by implementing such a remuneration scheme.

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Appendix 1

Selected Competitive Carrier Passenger Filings
In The United States¹

El Al, Isreali Airlines

Point-to-Point:	8%
Inclusive Tour Override:	3%
Volume Incentive:	\$40 per passenger (\$250,000 to \$1,000,000 annual revenues) \$50 per passenger (\$100,000 to \$5,000,000) \$60 per passenger (over \$5,000,000) \$30 per passenger (over \$50,000 on Holiday Class Economy Fares)

Japan Airlines

Point-to-Point	8%
Inclusive Tour Override:	3%
Bonus:	\$25 New-York-Tokyo One Way First Class New York-Tokyo one way Economy Class or Excursion
Volume Incentive	10% - 100 to 499 passengers per year 11% - 500 to 999 passengers per year 12% - 1000 to 1499 passengers per year 13% - 1500 to 1999 passengers per year 14% - 2000 to 2499 passengers per year 15% - over 2500 passengers per year

¹Commission levels such as these are applicable for payment to United States travel agencies only. Source: CP Air, Industry Affairs - Marketing, March 16, 1978.

Group Override/Tour Operator Plan:

12% 10 to 499 passengers per year
 13% 500-999 passengers per year
 14% 1000-1499 passengers per year
 15% 1500 or more passengers per year

Pan Am**Point-to-Point:**

8%

Incentive Tour:

3% for passengers originating in the United States

Volume Incentive:

To/From Rome, Brazil, Tokyo, Manila, Hong Kong or the Middle East

8% - 25 to 49 passengers
 10% - 50 to 74 passengers
 12% - 75 to 99 passengers
 15% - 100 or more passengers

Agent must earn a minimum of \$20,000 or 110% of last year's calendar quarter whichever is greater to qualify. Agent earns 1% extra for each 10% above last year's period or \$20,000 whichever is greater.

Group Override**Tour Operator Plan:****Tour Operator Support**

10% on U.S.-
 Europe/Africa/Middle East
 except Rome
 15% - U.S.-Rome
 15% - U.S.-Pacific
 10% - U.S.-South America
 5% - U.S.-Central America
 7.5% - West Coast-Hawaii up to 1800 local time
 10% - West Coast-Hawaii after 1800 local time
 10% - U.S.-Alaska
 10% - New York City/
 Dallas/Hawaii

Group Organizer Support Levels

{same as tour operator support except 7% West Coast - Hawaii