



FILE NO. 172/FLIGHT-KITCHEN/C&TA/CCP/2017
COMPETITION COMMISSION OF PAKISTAN
GOVERNMENT OF PAKISTAN

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POLICY NOTE

SUBJECT: AMENDMENTS IN THE CIVIL AVIATION AUTHORITY'S ORDER ON FLIGHT CATERING SERVICES AT CAA AIRPORTS

The Competition Commission of Pakistan (the '**Commission**') is mandated under the Competition Act, 2010 (the '**Act**') to ensure free and fair competition in all spheres of commercial and economic activity to enhance economic efficiency and to protect consumers from anti-competitive behavior. In pursuance of the clause (b) of Section 29 of the Act, the Commission is empowered to review policy frameworks for fostering competition and to make suitable recommendations to the Federal or Provincial Governments, to improve the conditions of competition in Pakistan.

2. In line with the aforementioned mandate of the Commission, this Policy Note recommends amendments to the Civil Aviation Authority Order dated 20th March 2018 *vis-à-vis* the Flight Catering Services at CAA Airports (the '**CAA Order**'), issued by Pakistan Civil Aviation Authority (the '**CAA**') under the Civil Aviation Authority Ordinance 1982 (the '**CAAO**') read with the National Aviation Policy 2015.

3. Earlier, CAA vide Tender dated 22nd April 2016 titled '*Tender Notice for establishment of Flight kitchen at joint venture basis at the new Islamabad international airport*', planned to establish a single flight kitchen at the New Islamabad International Airport ('**IIAP**') on a joint venture basis. The Commission received concerns and in order to assess the state of competition as a result of the

flight kitchen as advertised by CAA, open hearing was conducted on 22nd September 2016. After hearing all the stake holders, the Commission issued an opinion on 14th December 2016 (the '**Flight Kitchen Opinion**'). The Commission in Flight Kitchen Opinion observed that a single flight kitchen would only be justified if (a) there was a realistic plan to show that entry barriers created out of the exclusivity were balanced by technical or economic progress, a fair share of which was passed on to end consumers (b) due to the participation of the Regulator (i.e. PCAA) in the business, on a revenue sharing basis, a conflict of interest was created hence PCAA should consider alternate arrangements for the same and (c) at no point should any of the airlines be barred by the CAA to uplift meals from any off-premises option available to them¹.

4. On 16th January 2017, CAA while taking into account the recommendations of the Commission in the Flight Kitchen Opinion, invited the Airlines, Flight Caterers and Hotels to participate in an open tender for award of land space to establish non-exclusive flight kitchen facility at IIAP. Although, the Joint Venture Model was not incorporated in the tender document, however, an obligation of royalty per meal was imposed on the successful bidder i.e. USD 1.39 per meal on international routes and PKR 50 per meal on domestic routes. Meal royalty is essentially a tax levied by PCAA which is passed on, by the airlines/private catering company, to the final consumer. M/s Kitchen Cuisine (Pvt.) Limited (the '**KCL**') was awarded flight kitchen 01 after due tender process.

5. Subsequent to the award of tender, CAA vide its Order dated 20th March 2018 implemented a new policy i.e. **CAA Order**. The stated aims of the Order are (i) to ensure high standards of hygiene; (ii) to facilitate airlines and other catering providers to ensure establishment of high quality flight kitchen with competitive meal prices. In the CAA Order, two types of flight catering services have been introduced i.e. (i) outside CAA premises and (ii) inside CAA premises. The inside CAA premises

¹ Opinion on Competition Concerns in Establishment of Single Flight Kitchen in Islamabad International Airport on Joint Venture Basis by CAA, 14th December 2016.

has been further divided into two sub-categories i.e. (i) Airline/JV and (ii) Private Caterers.

6. Bare perusal of the CAA Order *vis-à-vis* the inside CAA premises flight kitchen reveals that for the Airlines/JVs the requirement of competitive bidding process is done away. The Airlines/JVs will be allotted space on the CAA premises on open space charges as an incentive. Whereas, the Private Caterers would have to acquire the space inside CAA premises after competing through open bidding process.

7. The position with reference to the meal royalties applicable to various undertakings engaged in the provision of flight kitchen services, both, outside and inside CAA premises is as follows:

Table 1 Applicability of Meal Royalty				
Meal uplift type	Outside PCAA premises	Inside PCAA premises		IIAP Kitchen Licensee No. 01
		Airline/JV	Caterer	
Meal to domestic route (@PKR 50/meal)	Not charged	Not charged	Not charged	✓
Meal to int'l route of Pakistani carrier (@US\$ 1.39/meal)	Not charged	Not charged	✓	✓
Meal to int'l carrier (@US\$ 1.39/meal)	✓	✓	✓	✓
Self-Catering domestic	Not charged	Not charged	NA	NA
Self-Catering Int'l	Not charged	Not charged	NA	NA

8. From the above table it seems that discriminatory treatment is meted out to the IIAP Kitchen licensee no.1 with reference to the meal royalty on domestic routes as well as international routes. **While the IIAP Licensee no. 1 is required to pay the royalty on international routes, including the local/Pakistani carriers' international routes, the Airline/JV are required to make the payment of royalty**

to the meals supplied to foreign carriers only. This essentially means that the local carriers including the Airline/JV operating the flight kitchen inside CAA premises are not obliged to pay royalty on meals supplied to its own airline or any other local/Pakistani airline operating on international route. Further, any private caterer operating from outside CAA premises is also exempt from the meal royalties on the meals supplied to Pakistani/local airlines operating on international routes. This discriminatory application of per meal royalties puts private caterers operating inside CAA premises, such as IIAP Kitchen licensee no.1 at a competitive disadvantage and *prima facie* distorts the level playing field in the relevant market of flight catering services.

10. Private caterers operating from inside CAA premises have to apply this royalty on provision of meals for all international routes (whether by local/Pakistani or foreign airlines) whereas the Airlines/JVs will apply this royalty only for meals to foreign airlines. For example, if a private caterer (located within CAA premises) provides meals to an international route operated by a local/Pakistani airline it would charge US\$1.39 per meal. However, if the same local/Pakistani airline operated its own kitchen and supplied to the same route no royalties would apply. Similarly, if this local/Pakistani airline supplied meals to an international route operated by another local/Pakistani airline no royalties would be applicable. The royalty would only be applicable if this airline supplied meals to a foreign airline for their international routes.

11. It is noted that airline operated flight kitchens and private caterers whether (located inside or outside CAA premises) compete with each other in the market for inflight catering services. This selective application of meal royalties renders private caterers (operating inside CAA premises) at a competitive disadvantage, since, it would be feasible for airlines to either (a) operate their own kitchens or (b) contract from companies located outside CAA premises as no royalties would be applicable on meal uplift from these sources. The inherent advantage given to Airlines/JVs arises not because of efficiency on their part but is rather due to the discriminatory application of meal royalty by CAA.

12. In addition to the above, the CAA Order provides incentives to Airlines/JVs for establishing a kitchen inside CAA premises which are not provided to private caterers. The relevant clauses are reproduced below:

Inside PCAA premises (Airlines/JV) – Clause D.2.4.9:

“As an incentive space may be allotted to airline/ Joint Venture on prescribed open space charges for an initial period of 10(ten) years and licensee will submit detail drawings/structural design for construction of infrastructure along with calculation of total cost of construction of the building infrastructure including fixtures & fittings (except moveable equipment/fixtures and fittings). PCAA will adjust the cost of construction on monthly basis in the following manner:-

Total cost of construction minus (difference of license fee as per actual status of land /building and open space charges)from the date of completion of construction.”

Inside PCAA premises (Private Caterers other than airlines) – Clause D.2.5.1:

“Tenders shall be invited through press for Flight Catering Service after wide publicity in leading newspapers. The reserve price of new catering set-up shall be evaluated on the basis of over & above PCAA prescribed open/covered/paved (as the space may be) rental charges. If licensee required additional land, rates will be charged on pro-rata basis”.

13. Based on various clauses of the CAA Order the difference in incentives offered to Airlines/JV versus private caterers can be summarized as follows:

- a) *Private caterers have to participate in a tender process as opposed to airlines/JV which can be granted space upon request (Clause D2.4.1);*
- b) *Private caterers have to pay a license fee over and above prescribed open/covered/paved space rental charges whereas, airlines/JV will be provided space on prescribed open space charges²;*
- c) *Cost of construction is adjusted for airlines/JV and not for private catering companies inside PCAA premises.*

14. It is noted that through the aforementioned incentives, airlines/JV are given an advantage over private caterers in terms of cost of establishment and operation of flight kitchen. Since all the players operate in the same market any incentives must be given equally so as to provide a level playing field to all.

15. The Commission observed in its Policy Note issued in the matter of complete ban on Establishment or Enlargement of Sugar Mills in the Province of Punjab³ that *“It needs to be appreciated that competition law is only a sub-set of competition policies, which simply put are a set of pro-competitive economic measures taken by the Government (be it relating to trade, labour or investment). The more robust these policies are; the better the enforcement of law and higher the chances of enhancing economic efficiency. The consumers stand to gain the most from greater competition. Competitive markets encourage more trade, lower prices; provide greater choice and more employment.”*

16. In the given circumstances, as detailed above, in order to create level playing field *vis-à-vis* the application of royalty, it is recommended that, CAA Order **may be suitably amended in accordance with the following:**

- (a). Royalty of USD 1.39 per meal be charged from Airline/JVs on the meals provided to local/Pakistani airlines for international routes;**
- or**

² Open space is land on which there is no construction and therefore, has lower charges as compared to covered or paved space.

³http://cc.gov.pk/images/Downloads/policy_notes/policy_note_complete_ban_on_sugar_08_06_12.pdf

(b). Royalty of USD 1.39/- per meal charged from private caterers located inside CAA premises, for the meal supplied to local/Pakistani airlines operating on international routes may also be waived.

17. Similarly, meal royalties of Rs. 50/- per meal for domestic routes may be applied uniformly on all operators whether airlines/JV or private caterer; or IIAP Kitchen No.1 licensee i.e. KCL may also be exempted from the same.

18. CAA may amend Clause 2.4.1 of the Order to make provision for tender for allotment of space in case of airline/JV in a similar manner to that applied on private caterers. Further, incentives with respect to adjustment of construction cost as provided to airlines/JV in Clause 2.4.3 of the CAA Order should also be provided to private caterers located in CAA premises, in order to create a level playing field.

Islamabad the 31ST day of December, 2018