



**UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION
OFFICE OF THE SECRETARY
WASHINGTON, D.C.**

Issued by the Department of Transportation
on the 30th day of July, 1997

Served: July 30, 1997

Applications of

NORTHWEST AIRLINES, INC.

Dockets OST-97-2145

UNITED AIR LINES, INC.

OST-97-2201

**for allocation of all-cargo frequencies under
the United States-Philippines Air Transport
Services Agreement (Route 2)**

ORDER TO SHOW CAUSE

SUMMARY

By this order we tentatively award Northwest Airlines an allocation of two weekly frequencies to provide all-cargo scheduled service in the U.S.-Philippines market for a period of one year from October 1, 1997.

BACKGROUND

U.S. Route 2 of the U.S.-Philippines Air Transport Agreement provides for scheduled combination service by designated U.S. carriers between the United States and the Philippines. The United States and the Philippines, however, signed a Protocol in 1995 that permits U.S. carriers to operate all-cargo services on Route 2 either by converting existing combination frequencies into all-cargo frequencies (but not back again to combination) or using new frequencies that become available based on an agreed timetable. The United States can designate only three U.S. carriers for Route 2, and we have designated Continental Micronesia (CMI), Northwest Airlines and United Air Lines. U.S. Route 2 carriers are currently limited to a total of 31 weekly frequencies. Those frequencies are allocated among the three designated carriers as follows: CMI-7,

Northwest-14 and United-10.¹ All the carriers are using their allocated frequencies. CMI and Northwest use all of their frequencies for combination service, while United is using its frequencies to operate seven weekly combination and three weekly all-cargo flights.²

Under the 1995 Protocol the frequencies available to U.S. carriers on Route 2 increase from 31 to 36 during a phase-in period between 1997 and 1999. Effective October 1, 1997, U.S. carriers will have the right to operate two additional frequencies, for a total of 33 weekly frequencies. Those frequencies are limited to the operation of all-cargo services. The frequencies increase to 34 weekly and 36 weekly frequencies effective October 1, 1998 and October 1, 1999, respectively, and remain at the 36 weekly level until September 30, 2003.

The Protocol also permits the United States to designate two additional carriers to provide all-cargo services on U.S. Route 3 of the Agreement.³ In addition, one U.S. carrier may be designated to operate a regional all-cargo service on Route 1b. Air Micronesia has been designated to provide that service.

APPLICATIONS

Northwest and United both request allocation of the two weekly Route 2 frequencies that become available on October 1, 1997, to provide all-cargo service between the United States and the Philippines.

Northwest proposes to operate twice weekly all-cargo service between Anchorage and Manila on the following routings: (1) Los Angeles-San Francisco-Anchorage-Osaka-Manila; and (2) New York-Anchorage-Narita-Bangkok-Manila (Bangkok is not served on the eastbound fight).⁴ Northwest proposes to operate this service with B-747F aircraft.

¹ CMI, Northwest and United hold certificate authority to serve the Philippines. See Orders: 95-1-41, 90-6-44 and 92-3-38, respectively. The frequency allocation of CMI was renewed and increased from four to seven flights when additional frequencies became available for regional service, and the frequency allocation of Northwest was renewed for fourteen frequencies. See Order 96-9-11. The frequency allocation of United was renewed for ten frequencies. See Orders 96-9-26 and 96-10-16. All of the allocations expire on September 30, 1998.

² We temporarily reallocated three frequencies that United had no plans to use until March 1, 1997, to Northwest to permit the carrier to provide interim all-cargo service in the U.S.-Philippines market. Order 96-10-16. Northwest ceased this service when United inaugurated its own all-cargo service using these frequencies.

³ U.S. Route 3 provides for scheduled all-cargo service between the United States via intermediate points and the Philippines and beyond. There are no frequency limits on services operated on Route 3. Federal Express was the only U.S. carrier providing all-cargo service on Route 3 before the 1995 Protocol. The Department, however, has recently granted new authority to Polar Air Cargo and United Parcel Service Company. See the *U.S.-Philippine All-Cargo Service Proceeding* in Docket OST-96-1074, Order 97-1-17. Northwest was an applicant in that proceeding.

⁴ Northwest filed a motion to amend its initial service proposal and United filed a motion opposing Northwest's request. United states that the Department should deny Northwest's motion because it is a
Footnote continued

In support of its application, Northwest states that it has demonstrated its commitment to the U.S.-Philippine market through the continuous use of its fourteen frequencies for combination service and the application for additional authority when it became available; that Northwest will represent a new all-cargo competitor in the U.S.-Philippine market and will serve four of the top five markets with single-plane service; that its heavy lift service will provide structural benefits, since only Polar would provide such service; and that it has extensive experience as an all-cargo carrier in the Pacific region.

United proposes to operate twice weekly all-cargo service between Anchorage and Manila via Tokyo with single-plane behind gateway service to Chicago and New York. It proposes to convert two DC-10 aircraft to all-cargo configuration to operate this service. United states that these flights would be in addition to United's three weekly all-cargo flights between Anchorage and Manila via Osaka, which began March 1.

In support of its application, United states that it has continuously used seven of its U.S.-Philippine frequencies to provide combination service, and since March 1997 it has used three of its frequencies for all-cargo service; that its service is offering valuable all-cargo competition between the United States and the Philippines; and that awarding the new frequencies to United will ensure a more equitable division of the available U.S.-Philippine frequencies.

RESPONSIVE PLEADINGS

Northwest and United filed answers to each other's applications and several subsequent pleadings.⁵

United states that Northwest is already the dominant U.S. carrier in the U.S.-Philippine market and that it is now seeking to pre-empt United's new challenge to Northwest's position as the dominant U.S. cargo carrier between the United States and Asia. United states that Northwest is not entitled to the frequencies merely because it applied for Philippine authority in the past, and that the Department has a policy of allocating frequencies to enable carriers to compete on a relatively equal basis. United also states

belated attempt to "raise the ante." Northwest replied that its motion is consistent with Department practice to permit amended proposals at any stage in a proceeding as long as other applicants' rights are not prejudiced and the decision here should be based on the proposal that it intends to operate. We will grant the motions for leave to file otherwise unauthorized documents and we will accept Northwest's amended service proposal as reflected above. It is true that as a general rule we do not favor revised service proposals in carrier selection proceedings where the revisions occur after the applicant submitting the revisions has been able to review the proposals of competing applicants. However, we find here that based on the nature of Northwest's revisions, their limited overall importance to our decision, United's full opportunity to comment on them, and our ability to weigh those comments, we find that United will not be prejudiced by our granting the motion to accept the amended service proposal.

⁵ Various pleadings by United and Northwest were accompanied by motions for leave to file. We will grant the motions.

that Northwest could convert two of its existing fourteen frequencies from combination to all-cargo service to operate its all-cargo proposal. United argues that Northwest wants to protect its existing combination services, but under similar circumstances involving United's proposed service to China, Northwest successfully opposed United's application and Northwest should not be exempt in this case from these same "frequency conversion" principles.⁶

With respect to the specific service proposals, United states that its proposal is superior because Northwest's proposal offers only one weekly turnaround service at Manila, since the second flight serves Bangkok in the westbound direction.⁷ United further states that it will serve the top five U.S.-Philippine city-pair markets either directly or through Anchorage connections five times a week. Finally, United argues that Northwest has not demonstrated the importance that its B-747F aircraft might have in this market compared to United's DC-10F aircraft, especially since Federal Express, the largest all-cargo carrier in this market, uses DC-10F aircraft.

Northwest states that over the past two years it has demonstrated its commitment to the U.S.-Philippine all-cargo market by seeking both the permanent reallocation of United's three then-unused frequencies and one of the new Route 3 all-cargo designations. Northwest states that none of these requests was successful, but that it did operate three all-cargo flights on a temporary basis until United inaugurated its all-cargo service. Northwest maintains that it is not the dominant U.S.-Philippine cargo carrier since the U.S. carriers on Routes 1 and 3 are not frequency restricted. Northwest states that it would be the new competitor in the U.S.-Philippine all-cargo market because United currently operates three weekly frequencies, while Northwest is precluded from serving without being compelled to convert its combination frequencies.⁸ Finally, Northwest argues that Manila is just as important to Northwest's Asia all-cargo service as it is to United's, which is why it seeks the all-cargo authority at issue here.

In addition, Northwest argues that, contrary to United's arguments, it cannot convert any of its fourteen weekly combination flights to all-cargo service because they operate at high load factors and must meet the competition from foreign carriers, and cannot use these combination flights to carry significant cargo because they carry a heavy volume of passenger baggage.⁹ Northwest states that United's reliance on the *China* case is misplaced because the Department did not base its decision on a formulaic approach, but instead considered consumer and structural benefits, benefits that also favor Northwest's application here.

⁶ See Orders 94-12-7 and 95-2-30.

⁷ Answer of United dated May 6, 1997, at 2-3.

⁸ Amended Application of Northwest dated April 21, 1997, at 3-4.

⁹ Consolidated Response of Northwest dated March 25, 1997, at 5-6.

Decision

After careful consideration, we have tentatively decided to allocate Northwest the two new weekly frequencies available October 1 to provide scheduled all-cargo service in the U.S.-Philippine market.

The 1995 Protocol provides valuable new opportunities to promote competition in the U.S.-Philippine all-cargo market. For several years, the United States was limited to all-cargo service by only one U.S. carrier. Based on the provisions of the 1995 Protocol, we recently authorized two additional carriers--UPS and Polar--to provide service on Route 3, and earlier this year, United elected to use the new combination frequency conversion provision to use three of its long-dormant Route 2 combination service frequencies to commence an all-cargo service in the U.S.-Philippine market. As we noted just a short time ago in the *U.S.-Philippine All-Cargo Service Proceeding*, the U.S.-Philippine all-cargo market is growing. Despite that growth, however, U.S.-carrier market share has declined significantly, demonstrating the critical role that could be played by licensing additional U.S.-carriers to provide more competitive all-cargo services.¹⁰ The two new frequencies that become available on Route 2 provide a valuable additional opportunity to improve the U.S. carrier share and promote further competition for U.S.-Philippine all-cargo services.

While both Northwest and United have presented proposals that would benefit the public, we tentatively find that the selection of Northwest better serves our goal of promoting competition in the U.S.-Philippine all-cargo market. Northwest would be a new entrant to that market. Not only would it offer new competition to United, but also new competition to Federal Express, Polar, and UPS. United, on the other hand, already serves the market with three weekly frequencies. While the allocation of additional frequencies to United would enable it to increase that service, the selection of Northwest will make available to the public new price, service, and aircraft options, a benefit we believe is especially important as the Philippine market develops. In these circumstances, we tentatively conclude that the competitive benefits of a new all-cargo entrant outweigh the competitive benefits of increased operations by United.

We also tentatively conclude that Northwest's proposal will maximize use of the limited frequencies available. Only two weekly frequencies are available for allocation at this time. Northwest proposes operations with B-747F aircraft; United proposes service with DC-10F aircraft. Northwest's proposal to use larger aircraft is an important consideration, since Northwest can provide greater capacity than United with the limited frequencies available. While United has argued that larger aircraft are not necessary in the Philippine market, it has not demonstrated why such aircraft services would be inappropriate and not benefit the market. We also note that Northwest operated B-747F aircraft in the all-cargo services operated during the period it held temporary authority to

¹⁰ Order 96-11-7, at 2.

use United's three dormant frequencies, and there is no indication that such service was not economic or that it produced excess capacity in the market. Contrary to United's arguments, the fact that Federal Express has chosen to use DC-10F aircraft in its all-cargo services is not determinative of the type of aircraft most suitable for Philippine all-cargo operations for each carrier on different routings providing different services. Federal Express operates a high frequency express type service and its operations are not subject to frequency limitations.¹¹ In this case, only two weekly frequencies are available for new all-cargo services on Route 2. We believe that the larger aircraft service will maximize use of the limited frequencies and provide greater benefits to general cargo shippers in the market.

With respect to the proposed routings in the carriers' service proposals, we tentatively conclude that the routings are generally comparable and thus do not warrant a decisional advantage for either carrier. Despite United's characterization, both carriers propose to offer twice weekly turnaround service between the United States and the Philippines via an intermediate point in Japan and on one westbound flight Northwest will also serve Bangkok. Both carriers would serve the top five markets either with single plane or on-line connecting service.

We believe that Northwest's intermediate stop at Bangkok will have little, if any, effect on the quality of its all-cargo service and, in any event, that effect is balanced by the fact that it will operate a larger aircraft in the market than would United. In this regard, we note that shippers of general cargo are typically less concerned than passengers about the inclusion of intermediate stops on a flight itinerary. Furthermore, Northwest will make the additional westbound intermediate stop on only one of its four directional flights. While this will increase the flight time by an additional eight hours, we find that this is not significant in this case given the nature of the traffic and that the dominant flow of traffic in the U.S.-Philippine market is in the eastbound direction.

Finally, as we noted in the *U.S.-Philippine All-Cargo Service Proceeding*, given the developing nature of the Philippine market, the carriage of some fifth-freedom traffic is likely to contribute to the overall success of cargo service between the countries.¹² Indeed, we note that United's existing U.S.-Philippine all-cargo operations, as well as those proposed in this proceeding, involve service via an intermediate point, demonstrating the benefit of support traffic as the Philippine market develops.¹³

We are unpersuaded by United's arguments that because Northwest already provides extensive all-cargo services between the U.S. and Asia, it should not be allocated the

¹¹ Order 96-11-7, at 6.

¹² Order 97-1-17, at 8.

¹³ United's three all-cargo flights operate over a Chicago-Anchorage-Osaka-Manila routing. One weekly flight also serves Los Angeles. *Official Airline Guide, Cargo Edition*, June 1997. See also, Application of United Air Lines, Inc., dated March 10, 1997, in Docket OST-97-2201, at 2.

frequencies at issue here.¹⁴ First, we conclude that the relevant market in this proceeding is the U.S.-Philippine market, not the U.S.-Asia market. As discussed above, given the growing nature of the U.S.-Philippine market, a primary goal in awarding the available frequencies is to increase the U.S. carrier competitive presence in that market. We have tentatively concluded that selecting a new carrier to provide all-cargo service will have the most beneficial impact on overall market structure and level of competition in the U.S.-Philippine market by increasing the range of price, service, routing, and aircraft alternatives available to shippers. Even if we were to consider the U.S.-Asia market to be relevant in this proceeding, given the limited number of frequencies available and the fact that United is already serving the market, we are not persuaded that the allocation of these frequencies would have a significant impact on either carrier's competitive posture in the region.

Finally, we are not persuaded by United's arguments that parity of Philippine frequency allocations should be the major decisional criterion in this case.¹⁵ Each allocation case is considered on its own merits based on a number of broad public interest considerations. Relative frequency levels is only one of several factors considered.

United cites the *U.S.-Argentina Combination Frequencies* case (Orders 94-9-36 and 95-2-23) and the *U.S.-China Frequency Allocation Proceeding*, (Orders 94-12-7 and 95-2-30) in support of its parity argument. As in this case, however, the relative frequency levels of the carriers applying for frequencies was only one factor considered. In the *Argentina* case the Department determined that the introduction of new service by American at New York provided greater service and competitive benefits than United's proposal to use the available frequencies to increase its service at Miami.¹⁶ In the *China* case, the Department concluded that competitive service in the largest U.S.-China markets--Beijing and Shanghai--as proposed by Northwest outweighed the benefits of United's proposed service to a new Chinese city. Furthermore, in the *China* case, the Department noted that United already held over half the total number of frequencies available to U.S. carriers and nearly three times the number of frequencies held by Northwest. In such circumstances, the Department concluded that increasing Northwest's allocation for combination services would promote competition in the combination service market, resulting in greater service options to the public.¹⁷

We are equally unpersuaded by United's argument that Northwest should convert some of its existing combination service frequencies to operate its proposed all-cargo service. Northwest has consistently used its combination frequencies and its operations have provided valuable services to the public and compete with the combination services operated by United and Continental Micronesia as well as foreign carriers serving the

¹⁴ Answer of United dated March 10,1997, at 2,4,5, and 7.

¹⁵ Answer of United dated March 10, 1997, at 2-4.

¹⁶ Order 94-9-36, at 3, and 95-2-23, at 3.

¹⁷ Order 94-12-7, at 6-7, and Order 95-2-30, at 4.

market. Since these frequencies cannot be reconverted, we see no reason why, in the circumstances of this case, the public interest would favor a result where Northwest converted its combination frequencies.¹⁸

Conditions

We have tentatively decided to subject the frequencies awarded in this case to a 90-day startup requirement and our standard 90-day dormancy provision once the service is inaugurated. The frequencies at issue here constitute valuable rights and we intend that they be used. We therefore tentatively conclude that imposition of these conditions is in the public interest.

ACCORDINGLY,

1. We tentatively allocate two additional weekly frequencies to Northwest Airlines, Inc. for all-cargo services in the U.S.-Philippine market through October 1, 1998, subject to a 90-day startup condition beginning October 1, 1997;
2. We tentatively conclude that the frequencies allocated in this proceeding, once inaugurated, should be subject to a 90-day dormancy condition;
3. We grant all motions for leave to file otherwise unauthorized documents in the captioned dockets;
4. We direct all interested persons to show cause why we should not issue an order making final our tentative findings and conclusions;
5. We direct interested parties having objections to our tentative findings and conclusions to file their objections with the Department, Dockets, attn.: Dockets OST-97-2145 and OST-97-2201, U.S. Department of Transportation, 400 Seventh Street, SW, Room PL-401, Washington, DC 20590, no later than August 11, 1997. Answers to objections shall be due August 18, 1997;¹⁹
6. If timely and properly supported objections are filed, we will afford full consideration to the matters or issues raised by the objections before we take further action. If no

¹⁸ We note that while United elected to use its dormant frequencies to inaugurate all-cargo services, it had not in fact been using its full allocation of combination frequencies, and thus the conversion in its case served to maximize use of valuable U.S. route rights.

¹⁹ The original filing should be on 8½" X 11" white paper using dark ink and be unbound without tabs, which will expedite use of our docket imaging system. We will authorize service by fax in this proceeding. All pleadings should include a fax number for service.

objections are filed, we will deem all further procedural steps to have been waived and will proceed to enter a final order;²⁰ and

7. We will serve this order on United Air Lines, Inc.; Northwest Airlines, Inc.; the Ambassador of the Philippines in Washington, DC; and the Department of State (Office of Aviation Negotiations).

By:

PATRICK V. MURPHY
Deputy Assistant Secretary for Aviation
and International Affairs

(SEAL)

²⁰ Since we have provided for objections to our tentative decision, we will not entertain petitions for reconsideration of this order.

MEGAN RAE POLDY
NORTHWEST AIRLINES
901 15TH STREET NW
SUITE 310
WASHINGTON DC 20005

DEPARTMENT OF STATE (EB/TRA/OA)
OFFICE OF AVIATION NEGOTIATIONS
ROOM 5930
2201 C STREET NW
WASHINGTON DC 20520

FEDERAL AVIATION ADMIN
AIR CARRIER BRANCH AFS-220
800 INDEPENDENCE AVE SW
WASHINGTON DC 20591

AMBASSADOR OF THE PHILIPPINES
1600 MASSACHUSETTS AVE NW
WASHINGTON DC 20036

JOEL STEPHEN BURTON
GINSBURG FELDMAN
1250 CONNECTICUT AVENUE NW
SUITE 800
WASHINGTON DC 20036