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Order 2002-2-8  
Served: February 11, 2002



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

Issued by the Department of Transportation  
on the 11<sup>th</sup> day of February, 2002

Essential Air Service at:

LAUREL/HATTIESBURG, MISSISSIPPI

under 49 U.S.C. 41731 *et seq.*

Docket OST 2001-10685 - 7

**ORDER TO SHOW CAUSE**

**SUMMARY**

By this order we are directing Express Airlines I, (Express) to show cause why the Department should not dismiss its claim for hold-in subsidy at Laurel/Hattiesburg, Mississippi. The carrier has requested annual compensation of \$2,222,783 for three nonstop round trips a day to Memphis with Saab 340 aircraft, the level of service we are requiring the carrier to provide.

**BACKGROUND**

On September 21, 2001, Express filed a 90-day notice of its intent to suspend its subsidy-free scheduled service between Laurel/Hattiesburg and Memphis, Tennessee, effective January 1, 2002. The carrier's service at the time it filed notice consisted of one nonstop round trip each weekday, and two daily one-stop round trips to Memphis over Meridian, Mississippi. By Order 2001-12-26, issued December 31, 2001, the Department prohibited Express from suspending service and required it to provide three nonstop or one-stop round trips each weekday and weekend to Memphis. That order also requested proposals from all carriers interested in providing replacement service, and we have received proposals from Express and from Corporate Airlines. Express is eligible for compensation for losses from January 1, 2002, until we select a long-term replacement carrier.

We have received two proposals from Express: one requesting \$2,222,783 for three nonstop round trips per day, seven days per week, to Memphis, and one requesting \$1,358,306, for two daily nonstops to Memphis. All of the service would be provided with Saab 340B aircraft, the smallest aircraft in Express's fleet.

## **DISCUSSION**

Express is a wholly-owned subsidiary of Northwest Airlines, Inc. (Northwest) providing feeder service to Northwest's Memphis hub under the label "Northwest Airlink." Express provides that service on a "fee-for-departure" basis. Under this arrangement, Northwest pays Express to provide service between Memphis and Laurel/Hattiesburg and, in turn, receives all revenues generated by Express. Presumably, Northwest has concluded that it no longer wants to pay Express to serve Laurel/Hattiesburg. However, we are not aware if this is because it is suffering actual losses under the fixed fee contract with Express, suffering opportunity losses by foregoing more profitable service elsewhere, or other reasons not related to the economic viability of the service.

Notwithstanding Express's fixed-fee contract with its parent company, its subsidy proposal is calculated as though Express were an independently-owned and -operated carrier. Thus, Express's hold-in subsidy proposal is based primarily on its costs of operating between Laurel/Hattiesburg and Memphis, less revenue calculated at \$63 per passengers.<sup>1</sup>

## **DECISION**

We have concluded that the methodology used by Express to calculate subsidy is not appropriate. Given the fixed-fee basis under which Express serves this market, Northwest, not Express, is the party that would sustain losses if revenue generated to and from Laurel/Hattiesburg were inadequate. The proper basis for determining subsidy need in this circumstance is not Express's expenses of operating between Memphis and Laurel/Hattiesburg less a prorated portion of revenue for passengers traveling beyond Memphis on Northwest. Rather, the proper basis for calculating subsidy need for such service is the effect that Express's service to Laurel/Hattiesburg has on Northwest's network profits. A majority of passengers that Express carries between Memphis and Laurel/Hattiesburg travel beyond Memphis throughout Northwest's domestic and worldwide systems. Thus, whether or not Express earns a profit on the Memphis-Laurel/Hattiesburg segment does not dictate whether that service turns a profit for Northwest's system. Indeed, since the cost of operating a spoke segment to a network hub may include most costs of moving passengers from the spoke city to points throughout Northwest's system, it is not unlikely that a carrier will suffer losses on the spoke segment while earning profits overall due to the flow traffic and revenue that spoke generates for the network.

Accordingly, we have tentatively determined to dismiss Express's subsidy claim for its hold-in service at Laurel/Hattiesburg.

This order is issued under authority delegated under 49 CFR 1.56(a)(f).

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<sup>1</sup> Express included estimates of some cargo and other revenue.

Accordingly,

1. We direct Express Airlines I, d/b/a Northwest AirlinK, to show cause why we should not dismiss its subsidy claim for forced service at Laurel/Hattiesburg, Mississippi, pursuant to Order 2001-12-26, pending the conclusion of the carrier selection proceeding; and
2. We will serve this Order on the Mayors of Laurel and Hattiesburg, the airport manager, the Mississippi Department of Transportation, the Governor, Northwest Airlines, Inc., and Express Airlines I.

By:

**READ C. VAN DE WATER**  
Assistant Secretary for Aviation  
and International Affairs

(SEAL)

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