

Posted: 1/10/2001

4:30 P.m.

Order 2001-1-6

Served: January 10, 2001



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

Issued by the Department of Transportation
on the 5th day of January, 2001

U.S.-CHINA AIR SERVICES (2001)

Docket OST-1999-6323- 2943

FINAL ORDER

Summary

By this order we make final our tentative decision in Order 2000-11-24, and award certificate authority and six weekly frequencies to United Parcel Service Company (UPS) for services in the U.S.-China market. We also make final our tentative allocations of two weekly frequencies to United Air Lines, Inc. and one weekly frequency each to Northwest Airlines, Inc. and Federal Express Corporation to expand their U.S.-China services.

Background

Currently three U.S. carriers, United, Northwest, and Federal Express operate air services between the United States and China. Collectively these carriers may operate a total of 44 weekly flights. United is currently allocated 19 weekly frequencies, Northwest is allocated 15 weekly frequencies, and Federal Express is allocated 10 weekly frequencies.

Under an April 8, 1999 Protocol between the United States and China, effective April 1, 2001, the United States may designate a fourth U.S. airline to serve China. The Protocol also provides for an additional 10 weekly frequencies that would be available for use by the four airlines that would then be designated to serve the market.

Four carriers, American Airlines, Delta Air Lines, UPS, and Polar Air Cargo applied for the new airline designation to serve China and frequencies to support their proposed services. In addition, the three carriers now serving applied for additional frequencies to expand their current operations in the market.

By Order 2000-11-24, issued November 21, 2000, we tentatively selected UPS to be the fourth airline authorized to serve China and tentatively allocated it six weekly frequencies for its services. In addition, we tentatively allocated the remaining four frequencies to the three carriers now serving with two frequencies allocated to United, and one each to Northwest and Federal

Express. Objections to the Department's tentative decision were due December 15, 2000, and answers to objections were due December 26, 2000.

Responsive Pleadings

All of the carrier applicants, as well as the City of Chicago (Chicago) and the City and County of San Francisco (San Francisco), filed responses to the Department's tentative decision. United, Northwest, UPS, Federal Express, Chicago and San Francisco filed answers. While certain commentors expressed disappointment with the Department's tentative decision, overall, no party objected to our proposed selection of UPS to serve China or our allocation to UPS of six of the 10 available frequencies. The only objections filed were from Northwest and Federal Express relating to our proposed allocation of the remaining four frequencies among the incumbent carriers.

UPS, United, and San Francisco filed comments in support of the Department's tentative decision and urge the Department to move quickly to make the decision final so that the carriers will have sufficient time to make the necessary arrangements for their services for an April 1, 2001 startup. UPS, in particular, urges the Department to issue a final decision no later than January 17, 2001, so that UPS will have sufficient time to complete the necessary regulatory procedures with the Chinese government to commence its services on April 1, 2001. In this regard, UPS states that Chinese government regulations require that UPS' application and supporting documents be received by CAAC at least 60 days prior to the startup of UPS' services, and that UPS cannot file its application until the Department issues a final decision in this case and it has been designated by the U.S. government. In order to meet these deadlines, UPS states that a final Department decision must issue no later than January 17, 2001. United as well as American, Delta, and Chicago urge the Department to seek a new agreement with China that includes a comprehensive opening of the market and that would avoid the expensive and time consuming carrier selection proceedings that the Department has had to conduct over the past few years.

American, Delta and Polar all express their disappointment with the Department's proposed selection of UPS, rather than themselves, as the new airline to serve China, but state that they will not object to the Department's decision. American and Delta further state that they are pleased with U.S. government efforts to expand code-share opportunities for non-designated airlines and state that they intend to pursue such arrangements with their Chinese code-share partners.¹ Chicago similarly states that it was disappointed by the Department's tentative decision and reiterates its support for American's Chicago-China services. It states, however,

¹ On October 20, 2000, U.S. and Chinese officials met in Seattle for informal aviation consultations. The two countries invited American Airlines and Delta Air Lines, the U.S. Carriers that have code-share arrangements with Chinese carriers but are not designated for direct service to China, to discuss with their Chinese code-share partners a type of wet-lease/code-share arrangement. Such an arrangement would involve the Chinese carrier leasing a plane and crew from its U.S. code-share partner to operate services authorized for Chinese carriers under the U.S.-China aviation agreement. If agreements to engage in this type of code sharing can be reached, American and Delta would be able to fly between the U.S. and China using their own aircraft and codes. Such agreements would be subject to approval by both governments.

that it will not object to the Department's order and expresses its support for American's planned services from Chicago with China Eastern under any new code-share opportunities.

Federal Express and Northwest filed objections to the Department's tentative decision to the extent that it did not grant each of them more of the available frequencies. Federal Express argues that it should have been allocated more of the available frequencies to expand its all-cargo services. In particular, Federal Express states that it should be allocated at least two of the remaining four frequencies because it is the only incumbent that is still unable to offer double-daily U.S.-China service. It further states that an award of all four of the remaining frequencies to Federal Express would best promote the competitive posture of U.S. businesses, as Federal Express is the only incumbent that offers the broad coverage of the Chinese markets and resources required to explore opportunities and to expand the presence of these businesses within the Chinese market. As a result, Federal Express states that granting it the four remaining frequencies would generate greater economic benefits to the United States than awards to either Northwest or United. Federal Express further argues that the Department's tentative decision to award three of the four frequencies to United and Northwest is contrary to the Department's conclusion that more cargo services are needed. Federal Express also states that it is concerned that the Department may not have had the opportunity to analyze completely the effect of the recent U.S.-China agreement allowing so called "zombie code-sharing." When combined with the proposed residual frequency awards in this case, Federal Express maintains that the residual awards effectively round out the incumbent carrier passenger service patterns at the expense of Federal Express and its customers. Finally, Federal Express argues that it has invested substantial amounts of time, money, and effort to build the service advantages it has today and that the Department should reward Federal Express' long standing commitment to the U.S.-China market with an award of at least two additional frequencies, and that anything less would be a disincentive to carriers contemplating being a catalyst to open new markets in the future.

Northwest states that it had requested a total of five frequencies for additional all-cargo and combination services, all of which it argues were supported by solid and realistic traffic forecasts. Nonetheless, Northwest states that the Department awarded it only one of the requested frequencies while United, which had requested two frequencies and presented a flawed forecast, received its full request. Northwest urges the Department to alter its tentative decision to award two frequencies to Northwest and one to United. Northwest maintains that there is a significant disparity between the frequency allocations of Northwest and United, with Northwest holding 15 frequencies and United 19. It maintains that a greater award to Northwest here would reduce the disparity and would increase competition in the U.S.-China market, consistent with the fundamental rationale of the Department's tentative decision to select a fourth carrier to serve China. Northwest states that with an award of two additional frequencies, it would have the flexibility to add one new all-cargo flight and one new combination frequency enabling it to increase its combination flights to offer a daily service to both Beijing and Shanghai, thereby providing stronger competition for United in the combination service market and addressing the need for more cargo capacity in the cargo market.

Northwest further states that Federal Express has provided no grounds for an award of all four of the remaining frequencies or to reduce the tentative allocation to Northwest; that awarding all

four frequencies to Federal Express would leave Northwest and United with no new frequencies; and that any award of more frequencies to Federal Express would serve only to cement Federal Express' existing dominant position. In response, Federal Express argues that, contrary to Northwest's allegations, the aggrieved party in terms of fairness is Federal Express, not Northwest. In this regard, Federal Express states that both combination incumbents can operate at least double-daily services, whereas Federal Express still cannot operate a double-daily service. Taking into consideration the combination services now provided and those that may be operated under the "zombie code-share" opportunities, there will be significant combination service competition without using the frequencies available here for additional combination services.

In its answer, United argues that neither Northwest nor Federal Express has offered any error in the Department's findings and conclusions or offered any new arguments that would warrant a change in its tentative decision to award United two frequencies and one each to Northwest and Federal Express. United states that in the 1999 U.S.-China Air Services case for allocation of the 17 additional frequencies available to incumbent carriers only, United received only five additional frequencies while Northwest and Federal Express each received six, even though United had sought a total of seven frequencies for a daily San Francisco-Shanghai service. United states that it started the San Francisco service with only five frequencies, notwithstanding the inherent difficulty of establishing a new service on a less-than-daily basis. United further states that it limited its request in this proceeding to achieving its goal of operating a daily nonstop service pattern between San Francisco and Shanghai, while Northwest and Federal Express were not focused on any particular service. In this regard, United states that Northwest has already announced that it will add an additional all-cargo flight and an additional combination service flight on April 1, 2001, of which one would use the new frequency and one would use an existing frequency. United argues that it is unclear therefore whether Northwest's additional combination service would be nonstop or one-stop and what market would be served and that such a late proposal should not be accepted. United further states that even if accepted Northwest has not demonstrated that its service would provide greater public benefits than United's proposal.

With respect to Federal Express, United states that Federal Express was granted sufficient frequencies for a "daily" cargo service in the last frequency proceeding. In addition, United argues that Federal Express has offered no specific proposal to demonstrate how or where it would operate either one or three additional frequencies. With fewer frequencies available than are required by carriers for their preferred service patterns, and eight of the ten available frequencies allocated to the benefit of cargo shippers, United claims that the Department reasonably decided that at least two should be allocated for combination services and that United's proposal offered the most benefits to consumers. United further argues that Federal Express conveniently overlooks the fact that none of its proposals would contribute to any increase in freight capacity eastbound from Asia to the U.S., but only to its intra-Asia services. In terms of the "zombie code-sharing" provisions, United argues that it cannot use "zombie" or any other code-share services to supplement its San Francisco-Shanghai services due to the restrictive nature of the U.S.-China air services agreement and that there is no basis to conclude that the "zombie code-share" services will be used for service in West Coast-China markets.

Finally, because the frequency awards to the incumbent carriers do not require Presidential review under 49 U.S.C. §41307, United urges the Department to issue a separate order relating to the frequency allocations to incumbents and sending a separate order regarding the uncontested selection of UPS for Presidential review. In this manner, United contends that the plans of incumbent carriers will not be delayed unnecessarily pending completion of the Presidential review process that can take up to 60 days.

San Francisco and Chicago support a final award of two frequencies to United and both urge that the Department affirm its tentative findings expeditiously so that the additional San Francisco service can be initiated successfully on April 1, 2001. San Francisco states that the San Francisco-Shanghai route is an asset for the entire nation, that the Department properly applied the decisional criteria in this case, and that none of the objections of Federal Express or Northwest have refuted San Francisco's unique ability to best use these frequencies.

Chicago states that an award of United's frequencies to either Federal Express or Northwest would further distort what is already a decision in favor of all-cargo service, and should, therefore, be rejected and that finalizing United's award in this case will maintain balance in the U.S.-China market.

Final Decision

We have decided to make final our tentative decision in Order 2000-11-24 and select UPS as the fourth airline authorized to serve China and allocate it six weekly frequencies for this service. We also make final our proposed additional frequency allocations to United, Northwest, and Federal Express.

Although the competing applicants for the new airline authorization have expressed disappointment with our tentative decision, no party has objected to our proposed selection of UPS to serve China or to our allocation of six weekly frequencies to UPS for its services. We therefore will make that selection final and will award UPS the necessary certificate authority and frequency allocation for its proposed services. The award to UPS will bring new all-cargo capacity to this valuable market. It will also provide consumers the benefit of carrier choice and a full range of competitive all-cargo services to the services now offered by Federal Express, as well as enhanced competition with the services offered by Chinese-flag carriers. This new airline service will serve our objective to increase the number of competitors in this market and to expand the range of price/service options available to consumers.

The principal objection to our tentative decision involved our allocation of the remaining four frequencies available on April 1 under the 1999 Protocol, with both Northwest and Federal Express contending that they should have been allocated more of the remaining frequencies. Both carriers have argued that such additional allocations to themselves would provide greater public benefits.

We have fully considered the arguments raised by Northwest and Federal Express and find that neither carrier has presented any new evidence or argument to warrant modifying our tentative allocations of the remaining four frequencies.

This case was instituted as the second phase of a major expansion of services provided for under the 1999 U.S.-China Protocol that enabled both sides to double the number of frequencies operated over a three-year period, and the allocations to incumbent carriers must be considered in the context of the overall expansion of services permitted. The first phase of the agreement enabled the three incumbent carriers to add 17 additional flights to the market. As a result of allocations made under the first phase of the agreement, Federal Express and Northwest each was allocated six additional flights and United was allocated five. In making those allocations, we recognized that the market had been restricted for many years and that all of the incumbent carriers had proposed services that would benefit the traveling and shipping public and respond to the pent-up demand for service. Collectively the incumbent carriers requested more frequencies than were available, reflecting the high demand for service and the need in both the cargo and combination segments of the market for additional new services. Recognizing the deficiencies in both segments of the market, we allocated the frequencies to ensure that all three carriers could expand their services and that both segments of the market would benefit.

The second phase of the agreement provides for an additional 10 frequencies available April 1, 2001, and the ability to authorize a fourth airline to serve the U.S.-China market. In our show-cause order and affirmed here, we have found that the public interest is best served by affording the public the benefit of another airline service, particularly in the all-cargo market, and by allocating that new airline sufficient frequencies to enable it to establish a viable service and a strong competitive presence in the market. At the same time, we recognized the continuing unmet demand for additional services from the incumbent carriers and the public benefits that would result from expanded services by each of them. Thus, as we had found in allocating the first phase of rights under the Protocol, we tentatively concluded that the remaining frequencies available should be used to enable all of the incumbent carriers to increase their services.

Taking into consideration the combined frequency awards in both proceedings under the Protocol, each of the three incumbent carriers would be allocated a total of seven weekly frequencies to expand its operations in the market to meet the demands for service. We believe that these overall allocations meet our stated objectives of ensuring that all of the incumbent carriers be able to make substantial use of the service expansions under the Protocol and that both the combination and cargo segments of the market benefit from those service expansions.

Both Northwest and Federal Express have renewed service and structural arguments made prior to our tentative decision in arguing now for greater awards to each of them. Federal Express contends that its cargo proposal offers greater economic benefits and that an award for all-cargo service is more consistent with the Department's show-cause order. Northwest claims that its various proposals are better substantiated and supported, warranting a greater award. Both argue that they should be allocated more frequencies so that they can be more competitive in the market, with Federal Express arguing that it should get more since the majority of U.S.-China frequencies are used for combination services, and Northwest arguing that it needs a greater allocation because it holds fewer overall frequencies than United.

We agree with both Northwest and Federal Express that additional services by both would benefit the public. However, having carefully reviewed all of these renewed arguments, we do

not find, upon reviewing the record as whole and the combined awards under the Protocol, that any party has made a persuasive showing that the overall public interest would be better served by increasing one carrier's allocation over another's in this case. Our combined awards to the incumbent carriers, taking into account both phases of the allocation, ensure that the combination and all-cargo segments of the market benefit from the service expansions now available and that all carriers serving can participate and compete substantially in the markets at issue. As we said in our tentative decision, with the awards in this proceeding United will be able to increase its current nonstop services in the San Francisco-Shanghai market, one of the largest U.S.-China markets, to a daily service and offer enhanced competition with the code-share services of Northwest and Air China from San Francisco. Northwest will be able to increase either its passenger or all-cargo services in the market. Federal Express will be able to expand further its existing all-cargo services that now serve three Chinese cities. We remain convinced that these allocations best serve the public interest and no party has provided any persuasive arguments that warrant modifying our proposed allocations.²

That said, and while the 1999 Protocol provided a valuable expansion of airline services in this important world market, we recognize that carriers now authorized to serve the market, as well as other carriers, including those that participated in this proceeding and were not selected, continue to be interested in serving China with new and/or expanded services. We intend to continue our efforts toward a more liberal aviation regime that would provide additional opportunities for airlines to serve this market.

Economic Authority

As we stated in our show-cause order, we will issue UPS a five-year experimental certificate of public convenience and necessity authorizing services between Anchorage, Alaska and Beijing and Shanghai, China, via Tokyo, Japan. We will require UPS to commence service no later than April 1, 2001, the date that the new authority becomes available under the 1999 U.S.-China Protocol.

The allocation of frequencies to UPS, as well as to United, Northwest, and Federal Express will be subject to our standard 90-day dormancy condition whereby the frequencies will become dormant and will revert automatically to the Department if they are not used for a period of 90 days. The 90-day dormancy period for the frequencies allocated to all four carriers will begin April 1, 2001, the date that the frequencies become available.³

² Contrary to Federal Express' argument, we find that these allocations are fully consistent with the tentative findings and conclusions in our show-cause order regarding all-cargo services. Indeed, at least seven and possibly eight of the 10 frequencies available for allocation in this proceeding will be dedicated to the provision of all-cargo services in the U.S.-China market.

³ We are not persuaded of the need to bifurcate our awards in this proceeding into two separate decisional orders.

ACCORDINGLY,

1. We make final our tentative findings and conclusions in Order 2000-11-24;
2. We select United Parcel Service Company and issue it, in the form attached, a certificate of public convenience and necessity, to provide scheduled foreign air transportation of property and mail between Anchorage, Alaska, and Beijing and Shanghai, China, via the intermediate point Tokyo, Japan;⁴
3. We allocate the 10 weekly frequencies at issue in this proceeding as follows:
 - UPS--6 weekly frequencies for the services authorized in ordering paragraph 1, above
 - United--2 weekly frequencies for services in the San Francisco-Shanghai market
 - Northwest--1 weekly frequency for any of the services proposed in this proceeding
 - Federal Express--1 weekly frequency for any of the services proposed in this proceeding;
4. The frequency allocations in ordering paragraph 3, above, are effective immediately for services commencing no earlier than April 1, 2001, and will remain in effect indefinitely, *provided that* the holder continues to hold the necessary underlying authority to serve the markets authorized; and *provided further* that the frequencies will become dormant and will revert automatically to the Department if they are not used for a period of 90 days;⁵
5. To the extent not granted, we deny all requests in the captioned proceeding;
6. Unless disapproved by the President of the United States under 49 U.S.C. 41307, this order and the attached certificate shall become effective upon the 61st day after its submission for section 41307 review, or upon the date of receipt of advice from the President or his designee under Executive Order 12597 and implementing regulations that he or she does not intend to disapprove the Department's order under that section, which ever occurs earlier;⁶
7. We will not entertain petitions for review of this order; and

⁴ We find that UPS is fit to provide the authorized services. UPS has previously been found to be a citizen of the United States and fit, willing, and able to provide scheduled foreign air transportation of property and mail as a certificated air carrier under section 41102 of Title 49 U.S.C. See, e.g., Order 99-12-7. We further find that issuance of the certificate granted will result in a near term increase in annual fuel consumption in excess of ten million gallons. As a result, our action constitutes a "major regulatory action" under the Energy, Policy, and Conservation Act of 1975, as defined by section 313.4(a)(1) of the Department's regulations. We find, however, that the service provided under the authority granted and resulting public benefits outweigh any adverse effects that may be caused by the increased fuel consumption.

⁵ The 90-day dormancy period with respect to the frequency allocation to each carrier will begin April 1, 2001.

⁶ This order was submitted for section 41307 review on January 5, 2001. **On January 10, 2001, we received notification that the President's designee under Executive Order 12597 and implementing regulations did not intend to disapprove the Department's**

8. We will serve this order on all parties to this proceeding; the Ambassador of the People's Republic of China in Washington, D.C.; the U.S. Department of State (Office of Aviation Negotiations), and the Federal Aviation Administration.

By:

SUSAN MCDERMOTT
Deputy Assistant Secretary for Aviation
and International Affairs

(SEAL)

*An electronic version of this document is available on the World Wide Web at:
http://dms.dot.gov/reports/reports_aviation.asp*



**Experimental Certificate of Public
Convenience and Necessity
for**

Route

797

This Certifies That

United Parcel Service Company

is authorized, subject to the provisions of Subtitle VII of Title 49 of the United States Code, the orders, rules, and regulations issued thereunder, and the attached Terms, Conditions, and Limitations, to engage in foreign air transportation of property and mail.

This Certificate is not transferable without the approval of the Department of Transportation.

By Direction of the Secretary

Issued by Order 2001-1-6

On January 5, 2001

Effective on January 10, 2001

SUSAN MCDERMOTT

Deputy Assistant Secretary for

Aviation and International Affairs

Terms, Conditions and Limitations

United Parcel Service Company for **Route 797**

is authorized to engage in scheduled foreign air transportation of property and mail:

Between the terminal point Anchorage Alaska, via the intermediate point Tokyo, Japan, and the coterminal points Beijing and Shanghai, the People's Republic of China.

This authority is subject to the following conditions:

- (1) The holder shall at all times conduct its operations in accordance with the regulations prescribed by the Department of Transportation for the services authorized by this certificate, and with such other reasonable terms, conditions, and limitations as the Department of Transportation may prescribe in the public interest.
- (2) The holder is not authorized to carry passengers (other than cargo attendants accompanying freight shipments).
- (3) The holder shall at all times conduct its operations in accordance with all treaties and agreements between the United States and other countries, and the exercise of the privileges granted by this certificate is subject to compliance with such treaties and agreements and with any order of the Department of Transportation issued under them. To the extent that the holder has authority to serve more than one country or points in more than one country on the same route segment, that authority does not confer upon the holder any additional rights (including fifth-freedom intermediate and/or beyond rights) in limited-entry markets unless the Department has completed any necessary carrier selection procedures to determine which carrier(s) should be authorized to exercise such rights and has notified the foreign country(ies) involved that any such selected carrier(s) has the required authority. In such cases, the fact that the carrier may hold authority to serve the countries (points) at issue on the same segment will not be considered as providing any preference to the holder in a carrier selection proceeding.
- (4) The exercise of the authority granted here is subject to the holder's first obtaining from the appropriate foreign governments such operating rights as may be necessary.
- (5) The holder's authority is effective only to the extent that such operations are also authorized by the Federal Aviation Administration (FAA), and comply with all FAA requirements concerning security.

(6) The holder shall at all times remain a "Citizen of the United States" as required by 49 U.S.C. §40102(a)(15).

(7) The holder shall maintain in effect liability insurance coverage as required under 14 CFR Part 205. Failure to maintain such insurance coverage will render a certificate ineffective, and this or other failure to comply with the provisions of Subtitle VII of 49 U.S.C. or the Department's regulations shall be sufficient grounds to revoke this certificate.

(8) Should the holder propose any substantial changes in its ownership, management, or operations (as that term is defined in 14 CFR 204.2(n)), it must first comply with the requirements of 14 CFR 204.5.

(9) In the event that the holder ceases all operations for which it was found "fit, willing, and able," its authority under this certificate shall be suspended under the terms of 14 CFR 204.7 and the holder may neither recommence nor advertise such operations unless its fitness to do so has been redetermined by the Department. Moreover, if the holder does not resume operations within one year of its cessation, its authority shall be revoked for dormancy.

(10) The holder acknowledges that this certificate is granted to determine if the holder's projected services, efficiencies, methods, rates, fares, charges, and other projected results will, in fact, materialize and remain for a sustained period of time, and to determine whether the holder will provide the innovative and low-priced air transportation it proposed in its application authority.

(11) The holder may combine services on this certificate with all services authorized by other Department of Transportation certificates or exemptions, provided, that such operations are consistent with the applicable bilateral aviation agreements; and provided further, that (a) nothing in the award of the route integration authority requested should be construed as conferring upon the holder additional rights (including fifth-freedom intermediate and/or beyond rights) to serve markets where U.S. carrier entry is limited unless and until the Department has completed any necessary carrier selection procedures to determine which carrier(s) should be authorized to exercise such rights; and (b) should there be a request by any carriers to use the limited-entry route rights that are included in the holder's authority by virtue of the route integration will not be considered as providing any preference for the holder in a competitive carrier selection proceeding to determine which carrier(s) should be entitled to use the authority at issue.

*As issued by
Order 2001-1-6
Route 797
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This certificate shall become effective **January 10, 2001.** It shall expire April 1, 2001; provided, however, that if the holder inaugurates service under this certificate on that date, the authorization will continue in effect until April 1, 2006, unless the Department earlier suspends, modifies or deletes the authority.

*This certificate is issued to reflect the award of new authority to serve the Anchorage-Beijing/Shanghai markets via Tokyo.