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

Issued by the Department of Transportation
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U.S.-U.K. Alliance Case

Docket OST-2001-11029 - 69

ORDER TO SHOW CAUSE

I. Summary

By this order, we tentatively grant, with conditions, the applications of American Airlines and British Airways and of United Airlines, bmi, and other foreign airlines that have an alliance with United for approval of and antitrust immunity for their respective alliance agreements. The conditions we propose include the divestiture of 238 weekly slots, coupled with access to necessary ground facilities, at London's Heathrow Airport, to support a total of 17 daily round trips by competing U.S. airlines. Of these, we expect American and British Airways to relinquish 224, to support 16 such services by competitors that we tentatively identify below, and bmi to relinquish 14, to support an additional daily round trip. The conditions also include an exclusion of immunity for certain traffic in the Dallas/Ft. Worth and Chicago to London Heathrow markets and in the Dallas/Ft. Worth to London Gatwick market.

The proposed action in this order is conditioned on reaching an agreement with the United Kingdom on an Open Skies aviation agreement. The proposed action will not be made final without that agreement. If an Open Skies agreement can be reached, our tentative decision would enable four U.S. carriers to enter the U.S.-Heathrow market for the first time, increase the operations of an existing carrier, and enable those five carriers to operate more than 6200 new annual nonstop roundtrips in that market. An Open Skies agreement would replace the existing aviation agreement between the United States and the United Kingdom, which now severely restricts the freedom of U.S. airlines to set their fares and to establish or modify service to London.

The tentative approval of antitrust immunity discussed in this order would apply to the Alliance Agreement¹ between American Airlines (American) and its wholly-owned affiliates and British

¹ The term "Alliance Agreement" as used in the application means (1) the joint applicants' agreement of August 3, 2001 (Exhibit JA-1), (2) any implementing or related agreements that the joint applicants conclude pursuant to the August 3, 2001 agreement to develop and carry out their alliance, and (3) any subsequent agreement(s) or transaction(s) by the joint applicants pursuant to the foregoing agreements. (Joint Application at 1, fn 1).

Airways Plc (British Airways) and its wholly-owned affiliates,² and to the Alliance Expansion Agreement and an Amended Coordination Agreement³ among United Air Lines (United), bmi British Midland Airways Limited (bmi), Austrian Airlines, Österreichische Luftverkehrs AG (Austrian), Lauda Air Luftfahrt AG (Lauda), Deutsche Lufthansa, AG (Lufthansa), and Scandinavian Airlines System (SAS) and their respective wholly-owned affiliates⁴ under 49 U.S.C. §§ 41308 and 41309.⁵ Under the agreements, the respective Joint Applicants will plan and coordinate service over their respective route networks as if there had been an operational merger among each set of carriers.

We tentatively find that our approval must be conditioned, as more fully explained in this order, on the introduction of competitive services by other U.S. airlines in their U.S.-London services. Our examination of the record supports a tentative finding that AA/BA should provide sufficient useable slots and facilities to permit 16 new daily Heathrow roundtrips, as follows: five to Continental, six to Delta, three to Northwest, and two to USAirways.⁶

In addition, the record shows that New York is the principal U.S. gateway to London. Accordingly, we propose that three of the slots allocated to Continental and three of the slots allocated to Delta would be specifically earmarked for New York service at Newark and JFK, respectively, and that one of the slots allocated to Delta would be earmarked for service at Boston. We propose that the slot to be divested by bmi would be allocated initially to United for service at Boston. Our proposed action accepts the Department of Justice's recommendation that Heathrow slots be allocated to allow flights by two new entrants in the New York market and two additional flights by competitors at Boston. In addition, the proposed action provides slots for nine flights by new entrants that are not earmarked for a particular market, which would give four U.S. carriers further opportunity to expand competitive service to London.

² American's named affiliates are TWA Airlines LLC, American Eagle Airlines, Inc. and Executive Airlines, Inc. d/b/a American Eagle. British Airways' named affiliates are British Regional Airways Limited, Brymon Airways Limited, CityFlyer Express Limited, and Deutsche BA Luftfahrtgesellschaft GmbH.

³ The term "Alliance Expansion Agreement" used in the application means a bilateral alliance agreement between United and bmi, which includes the following: the Alliance Expansion Agreement by and between British Midland Airways Limited and United Air Lines, entered into on September 5, 2001, the Marketing Cooperation Agreement by and between British Midland Airways Limited and United Air Lines entered into on November 8, 1999, the Code Share and Regulatory Cooperation agreement by and between British Midland Airways Limited and United Air Lines entered into on March 15, 2000 (previously filed with the Department in Docket OST-00-6954), as amended on January 16, 2001, any implementing agreements in furtherance of the foregoing agreements and any transaction undertaken pursuant to the foregoing agreements. The term "Amended Coordination Agreement" is used to describe a multilateral coordination agreement among the Joint Applicants and includes Amendment No. 2 to the Coordination Agreement dated September 5, 2001 (which amends the August 6, 1996 Coordination Agreement executed by United, Lufthansa, and SAS, as subsequently amended by the August 1, 2000 Amendment No. 1 to the Coordination Agreement, which added the Austrian Group to the original three-carrier alliance) in order to add bmi as a named party, any implementing agreements in the furtherance of the foregoing agreements and any transaction undertaken pursuant to the foregoing amendments. (United/bmi Joint Application at 2, Docket OST-2001-10575).

⁴ British Midland Regional Limited is a wholly-owned subsidiary of bmi and is included with bmi as an affiliate. Tyrolean Airways is a wholly-owned subsidiary of Austrian and is included with Austrian as an affiliate. Austrian also holds a majority interest in Lauda and the three carriers (Austrian, Tyrolean, and Lauda) will be identified as the "Austrian Group."

⁵ Hereafter the American/British Airways application will be referred to as AA/BA and the United/bmi, Austrian, Lauda, Lufthansa, SAS application will be referred to as United/bmi.

⁶ The slot numbers specified here and subsequently, unless the context indicates otherwise, refer to slot pairs, since each roundtrip flight requires an arrival and a departure slot.

We also propose to direct both sets of Joint Applicants to file all subsidiary and/or subsequent agreements with the Department for prior approval and to resubmit for review their alliance agreements in three years, rather than the five years directed in previous cases. If any of the Joint Applicants wish to operate under a common name or brand, they will have to obtain advance approval from the Department before implementing the arrangement.

As an express condition of the grant of antitrust immunity to the AA/BA Alliance and to the expanded alliance for United/bmi, we also propose to direct American and British Airways and United and bmi to withdraw from all International Air Transport Association ("IATA") tariff conference activities affecting through prices between the United States and the United Kingdom and for other markets described in this order. We further propose to direct British Airways and bmi to report full-itinerary Origin-Destination Survey of Airline Passenger Traffic data ("O&D Survey") for all passenger itineraries that include a United States point (similar to the O&D Survey data already reported by their respective partners, American and United).

We also propose to grant to AA/BA and United/bmi the necessary regulatory authorities, as tentatively set forth in this order, to permit the carriers to implement their proposed reciprocal, blanket code-sharing operations.

By this order, we are providing the Joint Applicants and other interested parties the opportunity to comment on our tentative findings.

II. Background

A. The United States-United Kingdom Aviation Markets

Almost 18 million passengers traveled between the U.S. and the U.K. in calendar year 2000, making the U.S.-U.K. our largest transatlantic aviation market. Just over 16 million of these passengers, or 92 percent, traveled between the U.S. and London, and 11 million of these passengers started or ended their trips in London.⁷

The two principal London airports for U.S.-London service are Heathrow and Gatwick. The U.S.-Heathrow market is larger than any other U.S.-Europe market. The U.S.-London market accounts for about one third of all transatlantic passengers, or about the same number of passengers as the next three largest European gateways combined. The U.S.-Heathrow market is nearly twice as large as the U.S.-Gatwick market.⁸

The New York-London market is significantly larger than any other U.S.-London market. It is also larger than most U.S.-country markets in Western Europe.⁹

⁷ Onboard passengers as reported in T-100 and T-100f reports and Origin & Destination Survey of Airline Passenger Traffic, adjusted to reflect information filed in the record of this case by American and British Airways, plus estimates for Virgin Atlantic, for Calendar Year 2000.

⁸ T-100 and T-100f data for Calendar Year 2000.

⁹ Onboard passengers as reported in T-100 and T-100f reports and Origin & Destination Survey of Airline Passenger Traffic, adjusted to reflect information filed in the record of this case by American and British Airways, plus estimates for Virgin Atlantic, for Calendar Year 2000.

B. Bermuda 2

The U.S.-U.K. aviation agreement (Bermuda 2)¹⁰ imposes severe restrictions on service and competition in the U.S.-London market. Bermuda 2 regulates market entry by limiting the number of airlines that may serve Heathrow, the number of cities that may receive nonstop service to London's Gatwick and Heathrow airports, and the number of airlines that may serve the authorized number of city-pair markets. Bermuda 2 controls airline capacity, and the United Kingdom has relied on those controls routinely to restrict U.S. carrier growth. Bermuda 2 also regulates the prices airlines may charge, and the United Kingdom routinely relies on those regulations to deny low fares from interior U.S. cities and to limit a connecting carrier's freedom to undercut nonstop carrier fares from gateway points.

As to Heathrow, the agreement permits only two U.S. airlines (now American and United) and only two U.K. airlines (now BA and Virgin Atlantic) to serve this London airport, and limits the number of U.S. cities that may receive Heathrow service. Consequently, no U.S.-Heathrow service may be provided by any other U.S. carrier serving London, or any other U.K. carrier.

Among the Bermuda 2 restrictions that most limit competitive initiatives are those on fares and fifth-freedom traffic rights. Fares are, with certain narrow exceptions, subject to approval by both parties, effectively requiring concurrence by not one but two governments to become effective, and our experience has been that innovative U.S. carrier fares from interior U.S. cities are routinely disapproved. Routes for the airlines of both countries are governed by detailed route schedules listing a limited number of intermediate and beyond points that are available for the exercise of fifth-freedom traffic rights; moreover, the use of the available points is subject to further severe limitations. The effect of this provision is largely to eliminate U.S. carriers from participating in markets between the United Kingdom and points beyond.

The net effect of Bermuda 2 restrictions is severely anticompetitive. It limits access to the largest London market; it interferes with the ability of the U.S. airlines that are not permitted to serve Heathrow to rely on pricing initiatives to compensate for this serious exclusion; it denies U.S. airlines basic operating flexibility, including, in particular, the ability to align their service with demand; and it prevents airline services from making a greater contribution to the growth and development of our economies.

In addition, the restrictions on fifth-freedom operations have severely restricted the ability of U.S. all-cargo carriers to integrate London into their global networks. Modern features, such as hub-and-spoke systems and open change-of-gauge opportunities, can also assume particular significance for these carriers. Under these circumstances, Bermuda 2's restrictions, particularly on fifth-freedom traffic, have been all the more onerous.

III. Applications

Two U.K. airlines, British Airways and bmi, have applied for immunity for alliances with two U.S. airlines, American Airlines and United Air Lines, respectively, in anticipation of an Open Skies agreement between the United States and the United Kingdom.¹¹ As a result of these

¹⁰ Agreement Between the Government of the United States of America and the Government of the United Kingdom of Great Britain and Northern Ireland Concerning Air Services, July 23, 1977, 28 U.S.T. 5367, T.I.A.S. No. 8641.

¹¹ The AA/BA applications were originally filed in Dockets OST-2001-10387 and OST-2001-10388. The United/bmi *et al.* applications were originally filed in Dockets OST-2001-10575 and OST-2001-10576. In

applications, and Open Skies discussions with the U.K. government, the Department has reason to believe that it may be possible to conclude negotiations with the U.K. that result in an Open Skies agreement between the two countries. An Open Skies agreement is a precondition to any grant of immunity in this case. If the negotiations are not successful, this show-cause order will not be made final.

A. AA/BA Joint Application for Antitrust Immunity¹²

On August 10, 2001, AA/BA filed a joint application seeking approval of and antitrust immunity for their Alliance Agreement, for at least a five-year term. They acknowledge that their application is premised on the achievement of an Open Skies agreement between the United States and the United Kingdom. They state that the Alliance Agreement establishes the contractual framework for comprehensive collaboration and coordination between the two carriers in a global alliance,¹³ and that if the agreement is approved and antitrust immunity and other regulatory authorizations are granted, the applicants will then proceed with implementation of more detailed operating accords that will provide for specific coordination/integration undertakings with respect to scheduling, marketing, pricing, planning, joint services, benefit sharing on certain routes, and related matters.¹⁴ They maintain that American and British Airways will retain their independent corporate and national identities, but following grant of antitrust immunity will be positioned to operate as if they were a single entity.¹⁵ Both American and British Airways are separately affiliated with several code-share and alliance arrangements, and AA/BA are founding members of the oneworld global alliance.¹⁶

AA/BA state that approval of this application will bring substantial benefits to consumers and communities in both countries and will enhance competition by enabling the applicants to compete more effectively with other immunized global alliances. They maintain that the alliance is pro-competitive and pro-consumer and will provide substantial new online service benefits and efficiencies when the hub-and-spoke systems of the two carriers are combined into a single, integrated network. They further maintain that the AA/BA alliance network will lead to an array

consolidating the applications, all parties to the cases were afforded a further opportunity to comment on the applications. Various procedural issues have arisen during our consideration of these applications, and we have made several rulings concerning the issues raised, and they are not repeated here. See Orders 2001-9-12, 2001-9-15, 2001-10-13, and 2001-11-10; also see Notices dated August 16, 2001, August 27, 2001, September 5, 2001, September 6, 2001, October 2, 2001, October 12, 2001, and November 15, 2001.

¹² The applicants also filed a joint motion for confidential treatment under 14 CFR 302.12 for certain information being submitted separately, and by Notice dated August 16, 2001, we granted immediate interim access to documents covered by the motion to counsel and outside experts for interested parties, consistent with conditions agreed to by the Joint Applicants and imposed by the Department in similar recent cases and as modified in subsequent orders. On August 27, 2001, the Department issued a Notice determining that the applications were substantially complete, but requiring American to submit an explanation of the methodologies it used in its submissions, and establishing further procedural deadlines. The August 27 Notice also noted that we would rule on the merits of the Rule 12 Motion of August 10 by subsequent order.

¹³ AA/BA Joint Application at 18.

¹⁴ The applicants separately filed a Joint Application for blanket code-sharing authorizations and related exemptions. (Docket OST-2001-10388) (See below) The Joint Services identified under the benefit-sharing blanket code-share arrangement are American's nonstop services between London and Boston, Chicago, Dallas/Ft. Worth, Los Angeles, Miami, New York (including Newark), and Raleigh/Durham; TWA's (and now American's after transition) nonstop services between London and St. Louis; British Airways' nonstop services between London and Boston, Chicago, Dallas/Ft. Worth, Los Angeles, Miami, and New York (including Newark); and British Airways' nonstop services between London and San Francisco. (AA/BA Joint Application at 18-19).

¹⁵ Id. at 3.

¹⁶ Id., Exhibits 14 and 15 and Id. at 72.

of service improvements, in addition to lower fares and new on-line services, on potentially 24,890 city pairs.¹⁷ These improvements include better schedule coordination for connecting flights leading to reduced elapsed time between departure and arrival, co-location to achieve gate proximity that will in turn improve connection time, coordination of luggage handling and transfer, improved passenger assistance at airports including the sharing of airport facilities (e.g. ticketing, transfer desks, and passenger assistance desks), and sharing of lounges or reciprocal access to lounges.¹⁸ They assert that the full public benefits to be offered by the proposed alliance cannot be achieved without antitrust immunity and that the alliance will (1) improve significantly consumer convenience and choice, (2) produce operating efficiencies that will create greater value for passengers and shippers, (3) increase competition in thousands of city-pair markets, and (4) generate economic benefits for communities across the worldwide networks of the two carriers.

AA/BA maintain that disapproval of their alliance agreement, or the prevention of its consummation by withholding immunity, would be inconsistent with the U.S. Government's commitment to Open Skies and to free and fair international competition.

AA/BA argue that it has been the Department's established policy to grant antitrust immunity with respect to agreements that are found not substantially to reduce or eliminate competition, if the Department concludes that antitrust immunity is required in the public interest, and that the parties will not proceed with the transaction absent antitrust immunity.¹⁹ In this regard, they maintain that the proposed alliance meets the public interest test, since the alliance will not substantially reduce or eliminate competition in any relevant market.

Specifically, in terms of the global market, they allege that their alliance will boost competition in the global air transport services market by creating an additional choice for consumers as well as enhancing competition in the international marketplace. They allege that the AA/BA oneworld alliance will not be the largest international aviation arrangement, but rather, that the Star alliance is the largest. AA/BA state that, in comparison to the Star alliance, oneworld will have less annual operating revenue, carry fewer passengers, serve fewer total destinations, account for fewer annual revenue passenger miles, have fewer aircraft, and have fewer employees.²⁰ Therefore, they maintain that the oneworld alliance offers a competitive scope of service to compete with the other global alliances.

In the U.S.-Europe market, AA/BA state that the Department recently noted that the U.S.-Europe marketplace is highly competitive, citing the service by eight U.S. airlines from existing hubs or in conjunction with an existing alliance, and service by 30 foreign airlines, principally from hubs in their homelands.²¹

For the U.S.-U.K. market, they maintain that effective competition will continue on these routes following implementation of the proposed alliance. They contend that this market is already "fiercely" competitive with nonstop service by more major carriers than any other U.S.-Europe market.²² They further argue that the "alliance will trigger a long-sought U.S.-U.K. open skies

¹⁷ Id. at 23, 34.

¹⁸ Id. at 23-24, and Ex. JA-2, 15.

¹⁹ Id. at 28.

²⁰ Id. at 35.

²¹ Id. at 35-36.

²² Id. at 36.

bilateral agreement. That, in turn, will allow substantial new entry, as well as permit an increase in the frequency of services offered by existing competitors. In addition to removing limits on capacity and on access to London's Heathrow Airport, an open skies agreement will eliminate pricing restrictions, thereby enhancing competition in beyond city-pairs."²³

The applicants acknowledge that they provide overlapping nonstop services, but argue that such overlap involves only six U.S.-London city-pair routes between London and New York, Boston, Chicago, Los Angeles, Miami, and Dallas/Ft. Worth. They argue that on all but one of these routes (Dallas/Ft. Worth-London), there is at least one additional competitor with nonstop service and one additional competitor with code-share service. They state that on the densest route, New York-London, there are already five other competitors providing nonstop service,²⁴ and that on most of the overlap routes, competitors also provide significant one-stop competitive service. Regarding the Dallas/Ft. Worth-London market, they note that there are highly competitive connecting routings offered by Continental Airlines, Northwest Airlines, United, and Air France, and there are numerous competitive connecting flights between Dallas/Ft. Worth and London that have desirable departure and arrival times, multiple weekly frequencies, and reasonable intermediate ground times.²⁵ In these circumstances, the parties maintain that their alliance will have no adverse competitive consequences and should be approved.

Finally, AA/BA state that grant of antitrust immunity should also cover the coordination of (1) the presentation and sale of the applicants' airline services in computer reservations systems, and (2) the operations of their respective international reservation systems. They also state that they will not proceed with the alliance without antitrust immunity.

B. UA/bmi Joint Application for Antitrust Immunity²⁶

On September 5, 2001, the UA/bmi joint applicants filed an application seeking approval of and antitrust immunity for an Alliance Expansion Agreement and an Amended Coordination Agreement, requesting that the antitrust immunity be made effective immediately upon the achievement of a new, liberal bilateral agreement between the United States and the United Kingdom, and that the authority remain in effect for a period of not less than five years.

Specifically, United/bmi seek approval of a bilateral alliance agreement between United and bmi (the "Alliance Expansion Agreement") and a multilateral coordination agreement among the Joint Applicants ("the Amended Coordination Agreement"). They maintain that approval of the

²³ Id.

²⁴ Continental, United, Virgin Atlantic Airways Limited, Air India, and Kuwait Airways provide nonstop service in the New York-London city-pair market and Continental and Virgin offer reciprocal code-sharing service. (AA/BA Joint application at 43; AA/BA Exhibit JA-8).

²⁵ AA/BA Joint application at 51; AA/BA Exhibit JA-8.

²⁶ On September 5, 2001, the United/bmi Joint Applicants (United, British Midland, Austrian Airlines, Lauda Air, Lufthansa, and Scandinavian Airlines System (SAS)) submitted their initial application, and on October 18, 2001, submitted additional documents and information to support their joint application. The submissions on October 18, 2001, were accompanied by separate motions of United, Austrian/Lauda, and Lufthansa for confidential treatment of portions of the material filed. On October 19, 2001, SAS submitted a motion for confidential treatment for documents it submitted under 14 CFR 302.12. By Notice, dated November 6, 2001, the Department granted immediate interim access to documents covered by the motion to counsel and outside experts for interested parties, consistent with conditions agreed to by the Joint Applicants and imposed by the Department in similar recent cases and as modified in subsequent orders. That Notice further stated that we would rule on the merits of the Rule 12 Motions by subsequent order. On November 20, 2001, the Department, in Order 2001-11-10, determined that the United/bmi applications were substantially complete and established further procedural deadlines.

Alliance Agreements will not reduce domestic competition in any relevant market. In terms of the global market, they state that the alliance will promote, not reduce, competition in the global marketplace. They further maintain that the proposed United/bmi alliance and its integration into the European Alliance will not substantially reduce competition between the United States and Europe, noting that virtually all transatlantic competitors are participating in alliances.²⁷ They maintain that including bmi in the European Alliance will further expand the alliance's reach in behind- and beyond-gateway markets in Europe, providing more consumers access to the competitive benefits generated by vigorous alliance competition. They argue that the proposed alliance will not reduce competition on United States-United Kingdom routes, that an immunized United/bmi alliance will pose no threat to competition, and that the alliance will be pro-competitive, because it will make possible bmi's entry into the London-U.S. market, at a time when a deregulated U.S.-U.K. bilateral aviation regime will finally allow new entry and enable existing competitors to expand their range of services. They further maintain that the proposed alliance will not reduce competition in any city pair, as bmi operates no transatlantic flights from Heathrow and United does not offer services with its own aircraft at Manchester, the only airport from which bmi offers service to the United States.²⁸ They note further that, even if bmi were thought to be a potential entrant in one or more of the U.S. city pairs that United currently serves nonstop, there would be no adverse impact from granting the carriers immunity because all of the city pairs are already competitive and will remain so.²⁹ United/bmi state that an immunized United/bmi alliance, and approval to integrate that alliance with the European Alliance, will increase competition in U.S.-U.K. and U.S.-Europe city pairs.

United/bmi also maintain that approving and extending antitrust immunity to the Alliance Expansion agreement will be in the public interest as it will enable United and bmi to integrate their networks at London Heathrow, operate more efficiently, establish a more integrated air transport system of U.S.-U.K. and beyond services via London through better network coordination, achieve economies of scope and scale, and enhance competition with other alliances. They state that they will be able to increase efficiencies, reduce costs, and provide better service to the traveling and shipping public in the following ways: expanded online networks; improved service in behind- and beyond-gateway city pairs; coordinated networks; wider availability of discount fares; inventory control; and reduced sales and marketing costs, as well as other efficiencies.³⁰

United/bmi state also that grant of antitrust immunity for the Amended Coordination Agreement would be in the public interest. They state that a coordinated United/bmi/Austrian group/ Lufthansa/SAS network will reach a broader range of consumers, offer greater efficiency gains, and promote more vigorous global network competition than could otherwise be obtained in the absence of antitrust immunity for the alliance. United/bmi acknowledge that all are members of the Star Alliance, a cooperative marketing alliance whose members compete on a global network

²⁷ United/bmi cite Air France, Alitalia, American, British Airways, Virgin Atlantic, Continental, Delta, Iberia, KLM, Northwest, Sabena, Swissair, Aer Lingus, and TAP Air Portugal (United/bmi Joint Application at 34).

²⁸ UA/bmi Joint Application at 38-39.

²⁹ bmi has stated that following the introduction of a new air services agreement between the U.S. and the U.K., it would wish to operate, in cooperation with United, services between London Heathrow and Chicago, Washington DC, Miami, Seattle, and Denver. (United/bmi Joint Application at 39 fn 60).

³⁰ United/bmi Joint Application at 42-45.

basis with other alliance groupings such as oneworld, SkyTeam, and Wings.³¹ They plan also to continue developing their code-share relationships with other Star Alliance member carriers.³²

Finally, United/bmi state that they will not implement the Alliance Expansion Agreement or the Amended Coordination Agreement without antitrust immunity.³³ They state that they have determined that they cannot and will not carry out the full range of joint activities in the London-U.S. and beyond markets contemplated by the Alliance Expansion Agreement and the Amended Coordination Agreement absent the protection from the threat of costly and burdensome private antitrust litigation afforded by antitrust immunity.

C. Joint Applications for Statements of Authorization and Related Exemption Authority

In connection with their alliance applications, AA/BA and United/bmi (and their affiliates) jointly applied for blanket statements of authorization under 14 CFR Part 212 and for related exemption authority under 49 USC §40109 in order to engage in reciprocal code-sharing operations.

Specifically, AA/BA and United/bmi seek statements of authorization and necessary underlying exemption authority for American to display British Airways' "BA" designator code in conjunction with foreign air transportation of persons, property, and mail on flights operated by American³⁴ and for United to display bmi's "BD" designator code³⁵ in conjunction with foreign air transportation of persons, property, and mail on flights operated by United, between (1) points in the United States; (2) points in the United States and points in the United Kingdom (either nonstop or via intermediate points in third countries); (3) points in the United States and points in third countries; and (4) points in the United Kingdom and points in third countries. The joint applicants also seek statements of authorization and necessary underlying exemption authority for British Airways to display American's "AA" designator code in conjunction with foreign air transportation of persons, property, and mail on flights operated by British Airways³⁶ and for bmi

³¹ The Star Alliance was formed on May 14, 1997, and now includes United, the Austrian Group (Austrian, Lauda and Tyrolean), bmi, Lufthansa, SAS, Air Canada, Air New Zealand, Ansett International Limited, Ansett Australia, All Nippon Airways, Mexicana, Singapore Airlines, Thai Airways International, and Varig Brazilian Airlines (United/bmi Joint Application at 47).

³² United/bmi Joint Application at 48.

³³ Absent immunity, the Joint Applicants state that the coordination necessary to achieve service improvements would expose the carriers to unacceptable antitrust risks. (United/bmi Joint Application at 44).

³⁴ Schedule 2 of the AA/BA code-share agreement, appended to the joint application, indicates that initially American will operate between Chicago and Manchester, Glasgow, and Birmingham, U.K. and between Raleigh Durham/St. Louis and London, carrying BA's code; and American and British Airways will operate between London, U.K. and Boston, Chicago, Dallas/Fort Worth, Los Angeles, Miami, New York, and Newark, carrying each other's codes. American will also operate between any route between a U.S. gateway and the following points: Albany, Albuquerque, Austin, Cedar Rapids, Cincinnati, Cleveland, Columbus, Des Moines, Dubuque, Duluth, Ft. Lauderdale, Ft. Myers, Indianapolis, Jacksonville, Kansas City, Las Vegas, Louisville, Memphis, Milwaukee, Minneapolis, Nashville, New Orleans, Norfolk, Pittsburgh, Rochester, San Antonio, San Juan, Springfield, St. Louis, Syracuse, and Tucson, carrying BA's code.

³⁵ United/bmi (Joint Application for OST-01-10576) indicates that United will place bmi's "BD" code on United's flights between London Heathrow and the coterminous points Boston, Chicago, Los Angeles, New York (JFK and Newark), San Francisco, and Baltimore/Washington DC and beyond those US gateway points to other US points served by United identified in Exhibit A to the United/bmi code-share application.

³⁶ Schedule 2 of the AA/BA code-share agreement, appended to the joint application, indicates that initially British Airways will operate any route between a U.K. gateway and the following points: Aberdeen, Belfast, Birmingham, Bristol, Edinburgh, Glasgow, Guernsey, Jersey, Manchester, UK; Vienna, Austria; Bahrain, Bahrain; Brussels,

to display United's "UA" designator code³⁷ in conjunction with foreign air transportation of persons, property, and mail on flights operated by bmi between (1) points in the United Kingdom; (2) points in the United Kingdom and points in the United States (either nonstop or via intermediate points in third countries); (3) points in the United Kingdom and points in third countries; and (4) points in the United States and points in third countries.

AA/BA and United/bmi state that their respective applications are premised on an open-skies agreement between the United States and the United Kingdom.³⁸ Both AA/BA and United/bmi maintain that blanket authorizations are in the public interest because they enable code-share partners to develop the full range of services permitted under applicable bilateral agreements, will provide a more efficient use of capacity in the marketplace, and will help maximize the range of service options available to the traveling and shipping public.

United/bmi request that the exemptions be granted for a minimum period of two years. Both AA/BA and United/bmi request that the statements of authorization be granted for an indefinite period, and be subject to the usual conditions, consistent with the Department's practice in other code-share proceedings.

D. Supplemental Information

On October 4, 2001, at the request of the Department, BAA, plc, the airport authority, and Airport Coordination Ltd, the slot coordinator, furnished information concerning access to slots and facilities at London airports.³⁹

According to the BAA, "generally, facilities are provided to airlines and to handling agents based on demand/market share, with facility agreements able to change to reflect changes in the patterns of demand between different airlines/handling agents." In order to operate a service on a new runway slot, "an airline requires a stand and terminal capacity in addition to terminal

Belgium; Prague, Czech Republic; Copenhagen, Denmark; Cairo, Egypt; Helsinki, Finland; Lyon, Marseilles, Nice, Paris, France; Berlin, Cologne, Dusseldorf, Frankfurt, Hamburg, Hanover, Munich, Stuttgart, Germany; Accra, Ghana; Bologna, Genoa, Milan, Naples, Pisa, Rome, Venice, Verona, Italy; Abidjan, Ivory Coast; Almaty, Kazakhstan; Nairobi, Kenya; Kuwait, Kuwait; Lilongwe, Malawi; Mauritius, Mauritius; Amsterdam, Netherlands; Oslo, Norway; Warsaw, Poland; Lisbon, Portugal; Doha, Qatar; Bucharest, Romania; Mahe Island, Seychelles; Cape Town, Johannesburg, South Africa; Stockholm, Sweden; Zurich, Switzerland; Dar es Salaam, Tanzania; Istanbul, Turkey; Entebbe, Uganda; Dubai, U.A.E.; Lusaka, Zambia; and Harare, Zimbabwe, carrying AA's code. Over transatlantic routes, (1) British Airways will operate between London and Atlanta, Baltimore, Charlotte, Denver, Detroit, Houston, Orlando, Philadelphia, Phoenix, San Diego, San Francisco, Seattle, Tampa, Washington DC and between Manchester, UK and New York, NY, carrying AA's code.

³⁷The United/bmi joint code-sharing application (Docket OST-2001-10576) does not specify the additional foreign points involving United's code on bmi services, but the joint applicants indicate that consistent with standard practice, they will notify the Department no later than 30 days before commencing any additional code-share services under the blanket statements of authorization requested to the extent that they are not specified in this joint application or previously approved applications.

³⁸ AA/BA code-share application at 1; United/bmi code-share application at 1.

³⁹ See, September 19, 2001, letter from Susan McDermott, Deputy Assistant Secretary for Aviation and International Affairs to Mr. Michael Toms, Group Strategy and Regulatory Director, BAA plc, and Mr. James Cole, Head of Coordination, Airport Coordination Limited. The information requested was electronically received, and on October 5 that information was placed in Docket OST-2001-10387, and was served electronically by the Department on parties to the proceeding. On October 16, 2001, corrections to the material were received, placed in the docket, and electronically served by the Department on the parties.

facilities, including a handler, check-in desks etc.”⁴⁰ BAA states that an airline receiving a slot, however, does not gain rights to specific terminal or gate facilities; rather these must be negotiated with the handler or airport operator and in some cases may take many months to be provided. While the BAA states that it would expect U.S. carriers wishing to set up operations from Heathrow to be able to obtain at least some slots through one form of slot ‘trading’ or another, the ACL notes specifically that primary trading slots, *e.g.*, auctioning of slots from the pool, is not allowed in the European Union.⁴¹

BAA estimates that “terminal and stand capacity constraints [at Heathrow] allow for six to ten new daily transatlantic services to begin operation in the first season [after an open skies agreement] and a further four daily transatlantic services at some point in the Summer 2003 season.”⁴² BAA states that this estimate, however, depends on airlines’ ability to obtain runway slot times. Moreover, BAA notes that stand availability depends on the terminal of operation for new wide-body service, with most terminals already at or close to maximum level for larger aircraft categories. BAA further notes that it does not have specific powers to direct airlines to relocate within and between terminals, but does initiate negotiation if relocation is required or desired. BAA expects only a few additional slots to be created at Heathrow, a small amount of which are expected in hours that transatlantic flights are currently being operated. It notes that new slots are likely to be departure slots and are unlikely to have accompanying arrival slots, which would be required to make new services viable. BAA anticipates that Terminal 5 will open in 2007, but expects that aircraft stands will be made available on the site on a phased in basis over the period 2004-2008. BAA further states that by 2008, it is planned that there will be 54 widebody and 3 narrowbody aircraft stands available on the Terminal 5 site.

With respect to the slots themselves, according to ACL, “priority is given to new entrants in the allocation of 50% of the pool, and to services seeking a year-round continuation of services started in the previous season. A proportion of year-round continuation requests will qualify as new entrants.”⁴³ ACL states that the Coordinator must allocate up to 50% of slots to new entrants and that the coordinator has no role in slot trading. It further states that there is no mechanism for slot leasing in the EU, and that AA/BA and their affiliates only hold slots used by them. It states that the objective of the slot allocation process is to try to achieve a fair allocation of slots to new entrants and incumbents in terms of both the quantity and quality of slots allocated. ACL notes that the pool is not split into new entrant and incumbent slot pools, but rather is allocated iteratively until a close to optimal solution is found. ACL states that carriers that do not have the necessary operating licenses at the time of application for slots are given a lower priority, and that “given the UK/US Air Services Agreement is a longstanding and complex issue, ACL would not be in a position to allocate slots to carriers prior to the completion of negotiations . . . [however] Provided a firm implementation date had been set and is imminent, it may be appropriate to allocate slots on a provisional basis.”⁴⁴ ACL states that when a carrier is allocated a slot, it is allocated a ‘package’ of runway, terminal, and parking capacity and that it is not

⁴⁰ The ACL defines slot as “the scheduled time of arrival or departure available or allocated to an aircraft movement on a specified date at an airport.” (Response of Airport Coordination Ltd, Appendix A at 1).

⁴¹ BAA Response at 1 and Response of Airport Coordination Ltd at 1.

⁴² BAA Response at 3.

⁴³ ACL Response at 4-5. ACL also states that the new entrant group of schedules is “subdivided between new airlines to the airport and new services requested by incumbent airlines but still qualifying as new entrants as they hold less than 4 slots per day.” New Incumbents are “all new slots requests by existing operators not qualifying as new entrants.” ACL Response, Appendix A at 3.

⁴⁴ ACL Response at 9.

possible to 'reserve' any element of this capacity in advance of the overall package. ACL states that other facilities (e.g., check-in desks, office and lounge accommodations etc) are determined by the BAA following the decision by the Coordinator to allocate a slot.

IV. Responsive Pleadings

Before the consolidation of the two antitrust cases, numerous parties filed answers and replies to the AA/BA application. All interested parties were also provided the opportunity to file answers and replies to both alliance/code-share applications after the Department consolidated the AA/BA and United/bmi applications.⁴⁵ The Dallas/Fort Worth International Airport, the St. Louis Parties,⁴⁶ the State of Maryland Aviation Administration, and Professors Alfred E. Kahn,⁴⁷ Jan K. Brueckner,⁴⁸ Janusz A. Ordover, Milena Novy-Marx,⁴⁹ and Mr. Daniel Kasper⁵⁰ support the AA/BA Joint Application. None of these parties takes a position on the United/bmi application. AA/BA filed in support of the United/bmi application, as long as their own antitrust application is also granted. United, bmi, and the American Society of Travel Agents support the AA/BA Joint Application only if certain conditions are met. Federal Express supports both applications, provided certain conditions are met. Continental Airlines, Delta Air Lines, Northwest Airlines,⁵¹ US Airways, Virgin Atlantic Airways Limited, the Houston Parties,⁵² the Cleveland Parties,⁵³ the New Jersey Parties,⁵⁴ and Charles A. Hunnicutt and A. Bradley Mims⁵⁵ oppose both alliance applications. The Air Carrier Association of America and the Memphis-Shelby County Airport oppose the AA/BA Joint Application. The Air Carrier Association of America and the Memphis-Shelby County Airport did not comment on the United/bmi Joint Application. In addition, the Department of Justice (DOJ) submitted comments in this proceeding.

⁴⁵ The "Initial Answers" to the AA/BA applications were filed November 2, 2001 and "Initial Replies" were filed November 9, 2001. In the consolidated proceeding, answers were filed December 17, 2001, and Replies were filed December 21, 2001. In addition to those parties discussed below, the applicants and other parties have submitted for the record numerous letters from congressional and civic persons and former DOT officials, supporting the carriers' positions in this case. Those letters are part of the record but are not enumerated here. Some other individuals, however, filed position papers that were not properly served on all parties to the proceeding, and, therefore, those papers are not part of the record and not reflected below. In addition, various parties filed numerous motions for confidentiality with their responsive pleadings, and these motions will be granted in this order. The motions for confidentiality filed by both sets of joint applicants with respect to their applications, however, will be addressed in a separate order.

⁴⁶ The St. Louis Parties include the City of St. Louis and the St. Louis Airport Commission.

⁴⁷ The Statement of Professor Kahn was prepared on behalf of American Airlines and British Airways and was served on all parties by American's counsel.

⁴⁸ Professor Brueckner states that the study provided was prepared for American Airlines and British Airways but that the underlying economic research was carried out independently, without airline support.

⁴⁹ The Joint submission of Professors Janusz A. Ordover and Milena Novy-Marx does not indicate whether it was submitted independently or at the request of a particular party.

⁵⁰ Mr. Kasper's statement was submitted at the request of American Airlines and British Airways.

⁵¹ In conjunction with their answers, Northwest Airlines, Continental Airlines, and Delta Air Lines each filed separate Motions for Confidentiality for portions of their submissions that make reference to confidential material filed by American and British Airways. We will rule on the confidentiality motions in a separate order.

⁵² The Houston Parties include the City of Houston and the Greater Houston Partnership.

⁵³ The Cleveland Parties include the Mayor of Cleveland and the Greater Cleveland Growth Associates.

⁵⁴ The New Jersey Parties include the City of Newark, the New Jersey State Chamber of Commerce, the New Jersey Alliance for Action, the New Jersey Business and Industry Association, and the Regional Business Partnership.

⁵⁵ Mr. Hunnicutt and Mr. Mims were formerly officials at the Department of Transportation.

A. Supporters

Dallas/Fort Worth, St. Louis, and the State of Maryland Aviation Administration argue that approval of the AA/BA application will foster increased consumer convenience and choices in travel at their respective airports as new competition by carriers will be possible on given routes and more passengers will be able to travel to Heathrow, the preferred choice of British airport for passengers. The State of Maryland and St. Louis argue that passengers will receive more benefits with Open Skies, since barriers will be removed that now preclude services to Heathrow from BWI in Maryland or from St. Louis. These parties also maintain that with Open Skies, American and British Airways will combine their hub and spoke systems to operate as an integrated network, and will thus be able to offer substantial new online services and efficiencies to passengers, and to encourage tourism. They state that approval of the AA/BA arrangement will increase competition on routes between the United States and the European continent, Asia, and Africa and will also permit a major source of competition available to passengers in Europe. They further maintain that by removing the severe restrictions associated with Bermuda 2 (the current U.S.-U.K. agreement), there will be freedom of entry by competing alliances and individual competitors. Dallas/Fort Worth, however, argues that it should not be carved out or excluded from antitrust immunity, as doing so would cause serious harm to the Dallas/Fort Worth community.

Dallas/Fort Worth also states that it takes no position on the United/bmi application because these alliance carriers have not indicated any intention to provide nonstop service between Dallas/Fort Worth and London.⁵⁶ Dallas/Fort Worth, however, states that it believes that approval of the application would enhance overall competition in the U.S.-U.K. market and would provide increased competition for AA/BA specifically.

Professors Brueckner, Ordover, and Novy-Marx state that the AA/BA alliance will provide more convenient seamless travel, a reduction in fares, as well as stimulation of demand, since now costs are higher because passengers often are required to interline in their travels and, that under the alliance the quality of service afforded passengers will be much greater. **Professor Kahn** also states that reversal of Bermuda 2 and achievement of open skies represent a culmination of more than 20 years of extending benefits of deregulation to the international arena. He states that “free entry is itself the best antidote to such market power [alliances] as might be created or reinforced by the union of two carriers, each of which may be dominant at its own domestic and international hub.”⁵⁷ **Daniel Kasper** states that he believes that competition and international aviation policy considerations support the grant of immunity sought by AA/BA. Mr. Kasper maintains that “even if they [opponents of the transaction] were unable to obtain sufficient slots from the slot pool, most of the carriers opposing AA/BA could obtain slots from their partners under alliances previously granted . . . immunity from the Department.”⁵⁸ He also states that “by removing existing bilateral restrictions on routing and pricing (i.e. deregulating), a U.S.-U.K. Open Skies agreement will make it easier for airlines to develop ‘secondary’ airports into even stronger competitive alternatives to LHR [London Heathrow]—as happened with U.S. airports . . . following deregulation.”⁵⁹

⁵⁶ December 17 Answer of the Dallas/Fort Worth Parties at 3.

⁵⁷ November 2 Statement of Professor Alfred E. Kahn at 5.

⁵⁸ December 17 Statement of Daniel Kasper at 5-6.

⁵⁹ Id. at 8.

United states that both the AA/BA and United/bmi applications are premised on the conclusion of an “open skies” agreement between the U.S. and the U.K. under which unlimited code sharing would be allowed in conjunction with the full integration of these alliances under immunity from the antitrust laws. United has no objection either to approval of the AA/BA alliance or to the code-sharing applications so long as the comparable applications of United/bmi are granted prior to, or at the very least, no later than that of AA/BA and becomes effective at the same time as the Open Skies agreement. United opposes, however, approval of the AA/BA code-share application in any third-country markets where there are agreed limitations on U.S. carrier code-sharing opportunities and no such opportunities are available. It also opposes approval in other markets where they propose to code share to third countries where there is a lack of reciprocity or where other issues have made it impossible for U.S. carriers to offer code-share service.⁶⁰

bmi maintains that the proposed AA/BA alliance should be granted antitrust immunity, but only subject to appropriate conditions that reflect the differences between the AA/BA and United/bmi alliances and that ensure reasonable access for all carriers for services between London and the United States. bmi notes that its alliance with United can over a period of time become a major competitive counterbalance to the AA/BA alliance between London and the U.S.; that it is best positioned to provide strong competition to counter the competitive concerns raised by the AA/BA alliance; and that by using bmi’s U.K. domestic and European network at London Heathrow to compete against British Airways’ extensive networks from both London Heathrow and Gatwick, the United/bmi alliance can provide consumers with an alliance network alternative to AA/BA.

Federal Express (FedEx) supports approval of both the AA/BA and United/bmi applications on the condition that the U.S. and the U.K. achieve a broad Open Skies agreement, including full change-of-gauge, routing flexibility, and fifth-freedom rights for cargo carriers. In this regard, FedEx states that the AA/BA alliance could create what will likely be the most extensive cargo network in the world. To compete effectively with U.K. carriers in U.S.-third country transshipment markets over the U.K., FedEx maintains that U.S. carriers must have full fifth-freedom rights. Accordingly, FedEx argues that the Department should condition approval of the alliance agreement on the entry into force of a bilateral agreement that meets all elements of the Department’s open skies definition, in particular, granting unrestricted rights to operate service between the U.S. and U.K. with no restrictions on serving intermediate or beyond points, change-of-gauge operations, routing flexibility, coterminization, or the exercise of fifth-freedom traffic rights, and ensuring that the liberal regime applies to cargo services.⁶¹ FedEx takes no position on the competitive impact that the alliance would have on combination carriers,⁶² but argues that physical constraints at Heathrow should not become an insurmountable barrier to liberalizing the U.S.-U.K. market.⁶³ FedEx “views with some skepticism the claims that, although slots may be available, matching facilities may not . . . Although towing aircraft from hard stands to remote parking to accommodate other aircraft is not an attractive option, it can be an effective answer to a lack of hard-stand capacity.”⁶⁴

⁶⁰ United cites the following as restricted points where AA/BA have proposed to implement code-share services beyond the U.K.: Istanbul, Turkey; Lyon, Marseilles, Nice, and Paris, France; Abidjan, Ivory Coast; Accra, Ghana; Cairo, Egypt; and Cape Town and Johannesburg, South Africa.

⁶¹ Initial Answer of Federal Express at 14.

⁶² Id. at 15

⁶³ Id. at 3.

⁶⁴ November 9 Reply of Federal Express at 3, n.3.

The **American Society of Travel Agents** argues that if the Department grants antitrust immunity to American and British Airways, immunity should also be conferred on travel agents who would be affected by aspects of the agreement.

B. Opponents

1. Basis for Opposition

DOJ supports DOT's long-time goal of replacing the Bermuda 2 bilateral with an Open Skies regime with no regulatory constraints on pricing and entry, and states that replacing Bermuda 2 with an Open Skies agreement would eliminate a number of significant legal restrictions on free and open competition in the U.S.-U.K. aviation market. DOJ notes that Bermuda 2 allows only four carriers (American, British Airways, United, and Virgin Atlantic) to provide any service between the U.S. and London Heathrow, and those carriers may serve only 10 U.S. cities from Heathrow. It also states that Bermuda 2 further limits the total number of U.S. cities that may be served from London's Gatwick Airport and also permits either government to place certain restrictions on capacity expansion in any U.S.-U.K. city pair, or to restrict carrier pricing in certain markets. Thus, DOJ states that, because achieving Open Skies is related to approval of an immunized alliance for British Airways, these immunity applications provide an opportunity to eliminate these legal restrictions and potentially enhance competition on many routes from the U.S. to London.

DOJ argues, however, that approval of the AA/BA transaction threatens a substantial loss of competition and higher prices for a large number of consumers. Therefore, without conditions to mitigate the harm, DOJ opposes approval of the AA/BA transaction. DOJ does not oppose including immunity for United/bmi transaction, without conditions, "as part of an otherwise beneficial trade." DOJ states that approval of the United/bmi alliance alone presents no appreciable harm relative to the status quo because bmi is not currently an actual or potential competitor in U.S.-London markets, as Bermuda 2 prohibits bmi from operating to the U.S. from its Heathrow base.⁶⁵

However, DOJ further states that approval of both AA/BA and United/bmi aligns the only two U.S. carriers currently permitted to operate at Heathrow (and that have slots and facilities to do so) with the two largest slot-holding carriers at Heathrow. In this regard, DOJ states that AA/BA are two of the four largest airlines in the world and two of the four largest competitors in markets connecting the U.S. and U.K.; that BA is the largest U.S.-London carrier by any measure, providing nonstop service to London on at least a daily basis from 21 U.S. airports; that BA serves London Heathrow from eleven U.S. airports with a total 26 daily frequencies; and that AA is the third-largest U.S.-London carrier in terms of cities served, and second largest in terms of frequencies.⁶⁶ DOJ also notes that in the summer 2001, United provided nonstop service to London on at least a daily basis from seven U.S. airports and that all of its London service is at Heathrow, which it serves with a total of 15 daily frequencies.⁶⁷ DOJ further notes that bmi is a regional airline, serving roughly 20 points in the U.K. and Europe from London Heathrow, and is the second largest carrier at London Heathrow in terms of slot holdings and daily operations after British Airways.⁶⁸ Thus, for Open Skies to provide significant consumer benefits, DOJ argues

⁶⁵ December 17 Public Comments of the Department of Justice at 3.

⁶⁶ Id. at 5-6.

⁶⁷ Id. at 8.

⁶⁸ Id.

that removal of the legal prohibitions of Bermuda 2 must be accompanied by meaningful access to Heathrow for other airlines serving the U.S.-London market. DOJ argues that failure to provide such additional access at London Heathrow would tend to “lock in” a market structure that is largely a product of Bermuda 2’s restrictions on competitive service.⁶⁹

DOJ further argues that entry into Heathrow remains constrained, increasing the anticompetitive impact of the alliances. DOJ cites evidence in the record as indicating that it will be very difficult for other carriers to obtain slots to begin or expand U.S. London Heathrow service, especially in the short run. It also argues that it is difficult to obtain aircraft parking spaces and terminal facilities necessary to operate new U.S.-London Heathrow service. Thus, DOJ maintains that even if other carriers can obtain arrival and departure runway space, airport authorities will refuse to allocate the slot if other facilities are unavailable, increasing the inability of other carriers to mount a competitive response to the alliances.⁷⁰ In this regard, DOJ states that under European Union slot allocation rules, new entrants (defined as carriers operating less than four slots on the day for which the slot is requested) get 50% of any slots available through capacity expansions or forfeited slots with the other 50% divided among incumbent London Heathrow carriers. DOJ states that carriers wishing to receive new entrant slots apply to the slot coordinator and are placed in the queue for carriers awaiting slots and DOJ states that new slots are allocated according to the carrier’s position in the queue.⁷¹

DOJ also does not believe that slots would otherwise be available through slot trades or slot transfers within alliances. Although straight slot sales are prohibited under European Union rules, slot trades are permitted, and DOJ states that a secondary market in London Heathrow does exist. It maintains, however, that the parties’ documents and other evidence demonstrate that it is difficult to purchase slots, particularly at peak times.⁷² DOJ further contends that obtaining slots through alliance partners is not a sufficient alternative to meet the competitive problems created by the alliance. Moreover, DOJ states that where some U.S. carriers are members of alliances with other carriers holding London Heathrow slots, it is unlikely that alliance partners will be the source of sufficient slots to support entry to ameliorate the competitive losses in the overlap markets, or to support significant levels of new U.S.-London Heathrow frequencies after Open Skies.⁷³ DOJ states that, in most cases, the Heathrow service currently provided by the alliance partners of U.S. carriers is extremely important to their networks, as London is a top business destination from almost every city in the world and competitive service is critical to partner alliances. Even assuming all slots from the “non-strategic” operations of alliance partners were made available for new U.S.-Heathrow service, DOJ contends that there are not enough such slots to move even existing Gatwick service to Heathrow, much less start new service to ameliorate competitive concerns. Moreover, DOJ states that most of the Heathrow service provided by the alliance partners is narrowbody service to Europe and not transferable to transatlantic operations. Finally, DOJ contends that additional barriers will deter entry into some markets. In particular, DOJ notes that entry by nonhub carriers is difficult in part because such a carrier does not have the connecting feed of the hub carrier and is forced to rely solely on local traffic.⁷⁴

⁶⁹ Id. at 5-6.

⁷⁰ Id. at 42.

⁷¹ Id. at 35-36.

⁷² Id. at 37.

⁷³ Id. at 40.

⁷⁴ Id. at 41-43.

With particular regard to AA/BA, DOJ maintains that the increased concentration by the proposed alliance can lead to higher prices through “coordinated interaction.” With fewer competitors, DOJ maintains that there will be less likelihood of a fare sale, or of discount offers targeted at large corporate travelers in the city pair, and greater likelihood that fare increases initiated by one competitor in the city pair will be matched by all other significant competitors in the city pair. DOJ contends that “the fact that there is a history of collusive activity in the industry belies the claims of AA and BA that coordination is unlikely.”⁷⁵ While AA/BA have submitted a “critical loss analysis” that purports to demonstrate that when combined the two carriers would not have the market power to raise fares unilaterally, DOJ argues that the carriers’ “analysis does not provide firm support for any conclusions about the ability of the immunized alliance to use market power to raise fares.”⁷⁶

Furthermore, despite the potential for benefits to interline passengers, DOJ contends that the AA/BA alliance differs from previous alliances in two important ways: unlike prior alliances, the competitive overlap markets in this case are significantly larger than the routes where connectivity benefits are likely, and secondly, the parties’ incentive to reduce capacity available for flow traffic may reduce any benefits that might otherwise accrue to connecting passengers from joining two airline networks together. DOJ states that such developments would contrast sharply with other alliances.⁷⁷ Thus, given the concentration and market power that would result from the AA/BA alliance and the entry constraints at Heathrow, if DOT decides to approve the AA/BA alliance (as well as United/bmi), DOJ states that DOT can and should impose conditions designed to reduce or eliminate the anticompetitive effects of the AA/BA transaction where possible.⁷⁸

Moreover, DOJ agrees with those that argue that Heathrow is a preferred airport, at least with respect to premium passengers, and rejects the AA/BA’s arguments to the contrary.⁷⁹ DOJ states that business passengers constitute a particularly high proportion of traffic to London; that the number of nonstop competitors directly affects prices paid in city pairs; and that connecting services do not discipline nonstop prices. DOJ further states that data on passenger choices show a strong preference for nonstop service among premium passengers and that “very few nonstop passengers paying business fares appear willing to substitute one-stop connection in most markets . . . and contrary to AA/BA arguments, . . . fewer than 1% of travelers on these routes choose to connect at any major European hub.”⁸⁰ DOJ notes that American and British Airways argue that increasing price sensitivity of corporate purchasers means that nonstop service is not a distinct market,⁸¹ but DOJ argues that the evidence on corporate travel policies supports a conclusion that nonstop service is a separate market.⁸² DOJ also states that airlines have substantial ability to price discriminate among passengers and that, contrary to AA/BA’s assertion,⁸³ “the proliferation of unpublished fares in fact increases the degree to which an airline can discriminate among customers by allowing the airlines to assess and respond on a case by case basis to a traveler’s price sensitivity.”⁸⁴

⁷⁵ Id. at 27.

⁷⁶ Id. at 29.

⁷⁷ Id. at 47.

⁷⁸ Id. at 49.

⁷⁹ Id. at 19-26.

⁸⁰ Id. at 12-14.

⁸¹ Citing AA/BA Joint Application at 54 (DOJ Comments at 15).

⁸² DOJ Comments at 15.

⁸³ Citing Joint Reply of AA/BA, Appendix B, at 3.

⁸⁴ DOJ Comments at 18.

Continental, Delta, and Northwest (opposing carriers) oppose the proposed alliances, particularly AA/BA. They argue that the proposed AA/BA alliance is unlike any other previously approved immunized alliance and raises unique and serious competitive and public interest issues.⁸⁵ Specifically, they state that the AA/BA alliance would represent a horizontal merger of the two largest competitors that would overwhelmingly dominate the largest and most important international market (U.S.-London and more particularly, U.S.-Heathrow). In this regard, they state that the alliance would create an entity that would control over 60% of the flights between the U.S. and Heathrow, 60% of the transatlantic peak arrival and departure slots at Heathrow, as well as 87% of the peak-hour slots.⁸⁶ They state that AA/BA control 584 of the U.S.-Heathrow slots and have 70% more U.S.-Heathrow departures and 50% more U.S.-Heathrow seats than all others combined.⁸⁷ **Continental** adds that AA/BA also control 50% of the entire U.S.-U.K. market, and an even larger share of the time-sensitive market.⁸⁸ **Delta** contends that AA/BA would dominate 15 major U.S.-London markets,⁸⁹ 9 U.S.-Heathrow markets⁹⁰ and that they are the only carriers on 9 U.S.-London routes.⁹¹ **Northwest** further states that on the six U.S.-Heathrow overlap routes, AA/BA have a market share ranging from a low of 37.5% in the Los Angeles market to a high of 100% in the Dallas/Ft. Worth market.⁹² Northwest also argues that under traditional merger guidelines, using the Herfindahl-Hirschman Index (HHI) of market concentration, the alliance will create certain highly concentrated markets. These include an increase of 1729 points to a level of 4388 in the U.S.-Heathrow market, and an increase of 1287 points to an HHI of 3327 in the U.S.-London market. At the extreme, Northwest points to the most extreme example of Miami-Heathrow, where the HHI would rise to the maximum possible of 10,000 points.⁹³

As a result, these carriers maintain that combining AA and BA services and distribution networks in the U.S., U.K., and Europe with their dominance at London would make it impossible for other airlines to compete effectively in any of these relevant markets and would adversely affect domestic competition. **USAirways** also argues that no antitrust immunity should be granted AA/BA or United/bmi unless and until there is sufficient competitive access

⁸⁵ “The American/British Airways combination on U.S.-London routes is so anticompetitive that no possible remedies can ensure effective competition on these routes, and competition on U.S.-U.K. and U.S.-Europe routes would also be adversely affected.” Initial Answer of Continental at 1. “There is absolutely no rational basis upon which the Department could conclude that the proposed alliance . . . should be approved.” Initial Answer of Northwest at 1. Some civic parties echo these positions. “[T]he proposed alliance would be exceptionally anticompetitive and should be disapproved.” Initial Reply of Cleveland at 1. “The Houston Parties oppose the joint applications in their current form, and urge the Department to deny them.” Initial Answer of Houston at 1. Memphis argues that the applicants need to “divest a large enough pool of LHR slots, at commercially viable times of day, to allow for truly competitive service at LHR.” Initial Reply of Memphis at 3. “The New Jersey Parties oppose the . . . alliance because it would drastically reduce, if not eliminate, airline competition between New Jersey and the United Kingdom . . .” Initial Reply of New Jersey at 1.

⁸⁶ Initial Answers of Continental at 19; and Delta at 14, and Exhibits DL-38 and DL-39.

⁸⁷ Initial Answer of Delta at 14, and Exhibits DL-29, DL-30, and DL-37.

⁸⁸ Initial Answer of Continental at 2, 19-20.

⁸⁹ The fifteen major markets identified are: Baltimore (BWI), Los Angeles, Boston, Chicago (ORD), Dallas/Ft. Worth, Denver, Miami, New York (JFK), Philadelphia, Phoenix, Raleigh-/Durham, St. Louis, San Diego, Seattle, and Tampa. Initial Answer of Delta at 14, and Exhibit DL-26.

⁹⁰ The nine markets identified are: Boston, Chicago, Detroit, Los Angeles, Miami, Newark (EWR), New York (JFK), Philadelphia, and Seattle. Initial Answer of Delta at 14, and Exhibits DL-25 and DL-27.

⁹¹ The nine routes identified are: Baltimore, Dallas/Ft. Worth, Denver, Phoenix, Raleigh-Durham, San Diego, Seattle, St. Louis, and Tampa. Initial Answer of Delta at 14, and Exhibit DL-33.

⁹² Initial Answer of Northwest at 14.

⁹³ Initial Answer of Northwest at 11-13.

for US Airways to serve Heathrow, access that includes commercially viable slots, and competitive groundside and related support activities.

Virgin Atlantic urges the Department to deny the AA/BA request for approval of, and immunity for, their proposed alliance. Virgin maintains that the result of AA/BA plans will be hubs for British Airways and American at both ends of their trans-Atlantic routes, which will greatly reduce the ability of companies to compete against them. Virgin argues that the two carriers are seeking to link the world's largest airline with Europe's largest carrier, the world's largest frequent flyer program with Europe's largest frequent flyer program, and the airline that dominates the most significant international airport in Europe with an airline that dominates large sections of the world's largest aviation market the U.S. domestic market. Virgin argues that "an alliance between British Airways and American will be much larger and more dangerous for competition than anything that has gone before."⁹⁴ Moreover, Virgin maintains that market growth for carriers seeking to operate North Atlantic services from Heathrow is all but impossible because Heathrow is full, and it disputes the applicants' contention that slots can be obtained relatively easily at Heathrow. Virgin states that, in fact, this contention is contrary to its own experience at Heathrow; that the owner and operator of Heathrow, BAA plc, has also recognized that Heathrow is effectively full; and that Airport Coordination Ltd (ACL), the independent body responsible for allocating slots at Heathrow, has said that accommodating new U.S. services at Heathrow will be very difficult.⁹⁵

The opposing carriers offer specific arguments with respect to various aspects of the alliances that they contend support their position that the proposed AA/BA alliance is anticompetitive and should not be approved. In this regard, the opponents argue that the AA/BA alliance would offer negligible network expansion benefits. **Delta** argues that American already "operates a comprehensive U.S.-London network with nonstop service to 21 of the top destinations in the United States, comprising 94 percent of total U.S.-London traffic."⁹⁶ **Continental** says: "Since British Airways is reducing its capacity at London Heathrow and eliminating smaller destinations and short-haul leisure routes, particularly at London Heathrow, connectivity benefits are shrinking."⁹⁷ **Northwest** further argues that, contrary to AA/BA's arguments, the clear objective of the alliance is not to link networks, but rather to control capacity and price in the six U.S.-London city-pair markets where the carriers' services overlap. In this regard, **Northwest** declares that "British Airways has adopted a strategy to 'de-hub' London Heathrow and to reduce the amount of connecting traffic flowing over Heathrow."⁹⁸ Northwest maintains that with such strategy, the alliance will not produce substantial new seamless connecting services for U.S. passengers as AA/BA allege.⁹⁹

In addition, many of the opponents identify certain key characteristics of the U.S.-London market, and argue that hubs in Continental Europe cannot provide effective competitive discipline for nonstop U.S.-Heathrow passengers.¹⁰⁰ **Delta** argues that the "lengthy backhaul

⁹⁴ Initial Answer of Virgin Atlantic at 113.

⁹⁵ Id. at 62-66.

⁹⁶ Initial Answer of Delta at 11.

⁹⁷ Initial Answer of Continental (public version) at 15. "British Airways has been reducing its capacity at London Heathrow to focus on lucrative point-to-point traffic and eliminate less lucrative connecting traffic." Id. at 27.

⁹⁸ Initial Answer of Northwest at 2.

⁹⁹ Id. at 2, 39-43.

¹⁰⁰ E.g., Initial Answer of Delta at 2, 12; Initial Answer of Northwest, Exs. NW-10, NW 11; Initial Answer of Continental at 24-26.

necessary to reach London from Continental European points renders the Joint Applicants' London hub effectively immune from one-stop competition."¹⁰¹ **Northwest** bluntly states that "one-stop service from the United States to Heathrow via points in Europe will not be effective . . . only three percent of all U.S.-Heathrow traffic connects over another point in Europe."¹⁰² **Virgin** claims that only 1.8% of U.K. passengers travel via third countries, and that "air travel products offered from London, in particular from Heathrow, do not generally compete with air travel products offered from other European hubs."¹⁰³ Moreover, according to Virgin, "only 14 percent of all passengers traveling between London and the 28 US cities served directly from London use indirect services."¹⁰⁴

Some opponents characterize Heathrow as greatly preferred to Gatwick for London passengers, to the extent that it should constitute a separate market for purposes of antitrust analysis. **Continental** describes Heathrow as "such a preferred airport that over 24% of U.S. carrier passengers in London Gatwick gateways chose connecting service to London Heathrow over nonstop London Gatwick service last year, despite the strong preference of passengers for nonstop service."¹⁰⁵ Indeed, Continental cites evidence in the record that Heathrow is the preferred London airport, that neither Gatwick nor Stansted is a substitute, and that even with the expansion at Heathrow (Terminal 5) there still will be insufficient access to Heathrow to meet demand. It also notes that British Airways has recently announced a possible withdrawal from BA's Gatwick base, and contends that the potential closing of BA's Gatwick base would eliminate all of the alleged connecting benefits at Gatwick and the argument that Gatwick is just as good as Heathrow.¹⁰⁶ **Northwest** also argues that the applicants' submission combines service to Heathrow and Gatwick, implying that Gatwick is a substitute for Heathrow. Northwest argues that London Heathrow has unique attributes and must be evaluated independently as a separate market.¹⁰⁷ Moreover, it notes that even if Heathrow and Gatwick were combined as a single aggregated market, the proposed alliance would result in dramatically increased levels of concentration that would also violate U.S. merger guidelines. In this regard, the New Jersey Parties note that DOJ's comments "confirm the New Jersey Parties' previous view that London Heathrow is a separate market and that London Gatwick is a poor substitute for London Heathrow."¹⁰⁸

The opposing carriers also contend that new entry in the London market is blocked by access constraints at London's Heathrow airport, as there are no commercially viable slots, gates, or airport facilities available. Virtually all the opponents argue a lack of available slots at Heathrow as a fundamental obstacle to competition, even with an Open Skies agreement. **Virgin** states, "there are no suitable slots available at Heathrow. None . . . British Airways has not been able to commence new Heathrow services other than by terminating existing services."¹⁰⁹ **Northwest** argues that there is not a "reasonable availability" of Heathrow slots.¹¹⁰ **Continental** argues that if AA/BA "really believed that London Heathrow slots and facilities were truly available, they

¹⁰¹ Initial Answer of Delta at 29, *citing* Exs. DI-20, DL-24.

¹⁰² Initial Answer of Northwest at 34. "The only U.S.-London nonstop market experiencing a significant amount of one-stop traffic is Dallas-London." *Id.* at 35.

¹⁰³ Initial Answer of Virgin Atlantic at 27, 91.

¹⁰⁴ *Id.* at 31-32.

¹⁰⁵ Initial Answer of Continental (public version) at 21 and Exhibit CO-18.

¹⁰⁶ December 17 Answer and Supplemental Comments of Continental at 20-21.

¹⁰⁷ Initial Answer of Northwest at 7-8

¹⁰⁸ December 21 Reply of the New Jersey Parties at 4.

¹⁰⁹ December 17 Answer of Virgin Atlantic at 4, 5-6.

¹¹⁰ December 17 Answer of Northwest at 5.

would be willing to give up slots and facilities since they could easily replace them.”¹¹¹ Should the Department determine to approve the alliances, the opponents offer remedies, which are couched in terms of slots and related access, as discussed below.

With regard to ground facilities, opponents cite BAA’s submissions at length: **Continental** argues that BAA’s and ACL’s submissions demonstrate that “new facilities for anyone but British Airways and its partners will not be built and . . . there would be substantial facility problems for new entrants at London Heathrow.”¹¹² **Delta** declares that “facilities at Heathrow are saturated . . . An important constraint is the inability to convert short-haul services to long-haul flights due to the substantially greater parking and other facility demands”¹¹³ **Northwest** notes that a “narrowbody slot/stand is of no use to a carrier that wants to commence transatlantic operations to Heathrow. . . . According to ACL, over 72% of the air transport movements at Heathrow are by narrowbody aircraft.”¹¹⁴ **Virgin** claims that “[u]ntil Heathrow’s Terminal 5 is approved, built, and opened, there is relatively little that can be done to relieve the aircraft parking and terminal capacity constraints.”¹¹⁵ **United** avers that ground-facility constraints at Heathrow, particularly at peak transatlantic periods, severely limit a carrier’s ability to transfer slots from narrowbody to widebody operations.¹¹⁶

The **Air Carrier Association of America** argues that strengthening two of the world’s largest carriers is contrary to the interest of domestic travelers, businesses and communities, and that the Department needs to first strengthen domestic competition before any decision can be made to allow the largest US carrier to expand its control of the US marketplace and to engage in discussions with Europe’s largest carrier about pricing, capacity, market control and CRS displays.

While most of the opponents comment primarily on the AA/BA alliance, some also comment on the effect of approving both the AA/BA and United/bmi alliances. **Continental** argues the public interest will not benefit by permitting “the four U.S. and U.K. carriers with the most coveted London Heathrow slots and facilities to combine, jointly set fares, and fix capacity, eliminate actual or potential competition with their partners and build fortresses at London Heathrow through *de facto* mergers. Allowing the four most dominant carriers at London Heathrow to merge into alliances while there are insufficient slots and facilities for any other carriers would be irresponsible.”¹¹⁷ It also maintains that the oneworld alliance of AA/BA and the Star alliance of United/bmi would put a “stranglehold” on the U.S.-London Heathrow routes and that the alliances would create a level of seat concentration in the U.S.-Heathrow market that would be greater than the seat concentration of the six largest U.S. carriers or combining the top 21 European airlines.¹¹⁸ Thus, **Continental** maintains that “no immunity should be granted unless truly open skies are achieved.”¹¹⁹ **Delta** argues that the U.S.-Heathrow incumbents have grown stronger and that the United/bmi alliance takes bmi and its Heathrow resources out of the running as a potential source of new entry, “further increasing the slot concentrations of the two alliances

¹¹¹ December 17 Answer and Supplemental Comments of Continental at 2.

¹¹² Initial Answer of Continental (public version) at 33.

¹¹³ Initial Answer of Delta at 21-22.

¹¹⁴ Initial Answer of Northwest at 24.

¹¹⁵ Initial Answer of Virgin Atlantic at 66.

¹¹⁶ Initial Answer of United at 4, n.4.

¹¹⁷ December 17 Answer and Supplemental Comments of Continental at 3-4.

¹¹⁸ *Id.* at 11.

¹¹⁹ December 21 Reply of Continental at 5.

and raising the added possibility of collective dominance.”¹²⁰ **Virgin** states that in its view “an AA/BA alliance would create a position of dominance for that alliance and Virgin Atlantic does not accept the arguments that AA and BA have put forward that the presence of United, bmi british midland and their Star Partners will in some way mitigate this anticompetitive position.”¹²¹ **Virgin** also argues that “there can be no doubt that the establishment of immunized alliances for AA/BA and UA/BD will create a position of joint or collective dominance.”¹²²

The **Cleveland Parties** and the **New Jersey Parties** also oppose both alliances, arguing that approval of alliances among the four largest slot holders at London’s Heathrow airport will foreclose competition at Heathrow and will further entrench these carriers at Heathrow, making it impossible for any other carrier to compete effectively with the alliances. **New Jersey** adds that in addition to dominating the market “an immunized AA/BA alliance would have the strongest sales and distribution networks in the U.S. and Europe, which would lead to further dominance.”¹²³ Both communities maintain that approval of the alliances would decrease service options and increase prices for U.S.-U.K. transportation at their communities, and, therefore, urge denial of the applications.¹²⁴ However, if the Department approves the alliances, both communities stress the importance of ensuring meaningful Heathrow access for other carriers for service to the Cleveland and the New York/New Jersey areas. They argue that this is particularly important for the economic development of their communities since Heathrow is the airport of choice for business travelers. **Cleveland** further stresses that “Continental’s proposed Cleveland-London Heathrow service would provide a new mid-western hub to compete with the American/United duopoly at Chicago and local passengers from throughout northeast Ohio and passengers connecting through Continental’s Cleveland hub would benefit from Cleveland-Heathrow service.”¹²⁵ Thus, absent “competitively viable, well-timed slots and facilities at London Heathrow,” both civic parties argue that the Department should not approve the proposed alliances.

The **Memphis-Shelby County Airport Authority (MSCAA)** similarly expresses concern about an immunized AA/BA alliance, notably that AA/BA will have an overwhelming dominance of the U.S.-London market, the largest such North Atlantic market by far. **MSCAA** states that AA/BA has the potential to shut out other carriers and gateways from any meaningful participation in the market, especially if there is no significant additional U.S.-London service by new-entrant carriers at London Heathrow and no real opportunity for service of other carriers via their Alliance hubs to act as a moderating factor against the dominance of AA/BA in the U.S.-Heathrow and U.S.-London markets. **MSCAA** states that it could support the AA/BA Alliance agreements if certain conditions were imposed upon, and accepted by, the joint applicants to allow additional new service by new-entrant carriers in the U.S.-Heathrow market, namely the joint applicants would be required to divest a large pool of Heathrow slots, at commercially viable times of the day, to allow for truly competitive service in the U.S.-Heathrow market.¹²⁶

Charles A. Hunnicutt and A. Bradley Mims in a joint statement adopt the arguments raised by Northwest against the alliances. They express concern that “the proposed alliances are likely to

¹²⁰ December 20 Reply of Delta at 3

¹²¹ December 17 Answer of Virgin Atlantic at 11.

¹²² Id. at 12.

¹²³ December 21 Reply of the New Jersey Parties at 3-4.

¹²⁴ December 21 Replies of the Cleveland Parties and the New Jersey Parties at 2 and 5.

¹²⁵ December 21 Reply of the Cleveland Parties at 4.

¹²⁶ November 9 Reply of the Memphis-Shelby County Airport Authority at 3.

harm competition and lead to higher fares for consumers in numerous U.S.-London and U.S.-Heathrow city-pairs,” and they maintain that “Heathrow is a distinct market, separate from service to Gatwick Airport.”¹²⁷ They argue that the problem with Heathrow is slot constraints that preclude entry to other carriers that could provide new competition in U.S.-Heathrow city-pair markets. They maintain that the U.S.-Heathrow markets are highly concentrated with AA/BA holding a 61% share of the Heathrow frequencies and the fact that American and British Airways are each other’s primary competitor in the U.S.-Heathrow markets. Thus, they argue the “barriers to entry represented by the slot constraints guarantee that the competitive effects of the alliance will go unchecked.”¹²⁸ Moreover, they argue that the AA/BA alliance is unlike any alliance the Department has ever approved, with an alliance between the two principal competitors in the largest U.S. international aviation market and “one not structured to provide primarily new end-to-end network service benefits” but rather one “to consolidate the positions of American and British Airways in overlap markets in which they are the principal competitors and to facilitate the reduction in capacity, at least by British Airways, in the overlap Heathrow markets.”¹²⁹

2. Remedies

For all these reasons, opponents argue that the AA/BA alliance is highly anticompetitive and should be disapproved; nevertheless, most suggest ways to ameliorate the anticompetitive effects, should the Department approve the alliance.

Continental, Delta, and Northwest argue that the only basis on which the which the Department should continue to process the AA/BA application would be: (1) an agreement on full open skies between the U.S. and the U.K. and beyond the U.K., including beyond London (Heathrow); (2) the immediate and permanent divestiture by AA/BA of sufficient Heathrow slots to discipline the alliance under open skies; and (3) the allocation to U.S. carriers of commercially viable facilities at Heathrow to accommodate the operational and customer service requirements of new U.S. carriers services. In this regard, **Delta** argues that 504 weekly Heathrow slots during the peak transatlantic window are “the minimum necessary to begin to challenge” the alliance, representing 36 daily round trips.¹³⁰ Of these, Delta states that it would need 11 daily flights: 4 daily round trips from New York (JFK), 3 serving Atlanta, 2 at Cincinnati, and 1 at Boston. **Continental** argues that it would need sufficient slots to operate a total of 10 daily roundtrip flights, with six roundtrips from New York/Newark, 3 roundtrips from Houston, and 1 roundtrip from Cleveland.¹³¹ Continental maintains that it has a particularly critical stake in the proposed alliance because Continental serves more U.K. points from the U.S. than any other airline and has no immunized alliance with a European carrier.¹³² **Northwest** argues that a total of 448 weekly slots during commercially viable time periods would need to be divested.¹³³ Of these,

¹²⁷ December 19 Joint Statement at 2.

¹²⁸ *Id.* at 3.

¹²⁹ *Id.*

¹³⁰ Initial Answer of Delta at 24. Delta also argues that at a minimum the 24 daily flights recommended by DOJ in 1998 would be necessary to ensure *de facto* open skies, but states, however, that it has demonstrated slots sufficient to fund at least 36 new daily Heathrow flights would be needed to competitively counteract the Heathrow alliances. December 21 Reply of Delta at 3.

¹³¹ Initial Answer of Continental at 46-51.

¹³² Initial Answer of Continental at 3.

¹³³ Initially, Northwest maintained that 420 slots would need to be divested (Initial Answer at 35); however, Northwest modified its estimate after other carriers responded to the number they would need. In its December 17

Northwest states that it would use its slots to operate 7 daily roundtrips to be served from Detroit, Minneapolis/ St. Paul, Memphis, and Seattle.¹³⁴ The carrier further claims that arrival slots need to be timed between 0500 and 1059, with departure slots between 1000 and 1559.¹³⁵ Northwest goes on to say that “anything short of [448 slots] would ignore good faith explanations of new service requirements and would fail to meet the public interest standard governing this proceeding.”¹³⁶ Northwest also argues that, of the 745 slots in the commercially viable transatlantic window that are not held by incumbents or their alliance partners, 528 are linked to facilities that are not suitable for wide-body aircraft.¹³⁷

USAirways states that it must be able to operate 2 daily roundtrip flights from Philadelphia, and 1 daily round trip each from Pittsburgh and Charlotte.¹³⁸ USAirways emphasizes that it is critically important that approval of the alliance be conditioned upon the creation of a truly competitive market structure in which smaller independent carriers can effectively compete with their bases of operation. **Memphis** calls for at least 238 weekly slots to be divested, the minimum “to cover the current level of service operated at London/Gatwick (LGW) by Continental, Delta, Northwest and USAirways . . . a better estimate . . . is Northwest’s suggestion of 420 slots.”¹³⁹ **New Jersey** calls for “no limits” on the number of slots available to competitors, but emphasizes the need for slots and facilities to support service at Newark/New York.¹⁴⁰ In this regard, New Jersey notes that Continental would need slots and facilities for at least six daily nonstop flights between its Newark hub and Heathrow.¹⁴¹ **Cleveland** argues that it is imperative that the Department reallocate slots “sufficient to allow Continental to institute new Cleveland-London Heathrow service.”¹⁴²

In the context of the slot divestiture, opposing parties argue that American and British Airways should not decide which slots that they will divest to new entrants and that the U.S. new entrants will need fair and impartial procedures to secure and transfer competitive slots and facilities. **Northwest** counters the contention of AA/BA that U.S. carriers can obtain all the slots they need from their foreign carrier alliance partners who currently serve Heathrow, noting that the applicants have presented no factual evidence that alliance partners are prepared to provide their Heathrow slots for use by U.S. carriers.¹⁴³ Concerning slot divestiture, **USAirways** maintains that the Department must require divestitures not only from AA/BA but from UA/bmi as well, arguing, “it would be inexplicable to require only half of the duopoly to divest the slots and facilities necessary to create a competitive market structure under open skies. Rather, UA-BD’s [bmi’s] large slot holdings must be part of the competitive solution that provides new entrant access to Heathrow.”¹⁴⁴

Answer, Northwest states that to accommodate all carrier requests, there would need to be 98 slots for Northwest, 154 for Delta, 140 for Continental and 56 for USAirways.

¹³⁴ Initial Answer of Northwest at 35.

¹³⁵ Initial Answer of Northwest at 24, *citing* Ex. NW-30.

¹³⁶ December 21 Supplemental Reply of Northwest at 8.

¹³⁷ Initial Answer of Northwest, at 27 *citing* Exs. NW-31, NW-39.

¹³⁸ December 14 Answer of USAirways at 3 and 7.

¹³⁹ November 9 Reply of Memphis at 3.

¹⁴⁰ November 9 Reply of New Jersey at 7 and 9.

¹⁴¹ December 21 Reply of New Jersey at 5-6.

¹⁴² December 21 Reply of Cleveland at 1-2.

¹⁴³ Initial Answer of Northwest at 31.

¹⁴⁴ December 21 Reply of USAirways, at 3.

DOJ notes that AA/BA compete on a nonstop basis in six city pairs and maintain that approval of the AA/BA alliance would significantly increase concentration in the New York-, Boston-, Miami-, Chicago-, and Los Angeles-London Heathrow markets, and that in each of the markets, except Los Angeles, the parties' combined shares of both frequency and time-sensitive business passengers exceed 50%.¹⁴⁵ DOJ argues that AA/BA command a much larger share of the lucrative premium market than their share of all passengers would suggest, noting that American and British Airways are the number one and number two carriers of time sensitive passengers (as measured by premium traffic) in five of the six overlap markets.¹⁴⁶ Thus, DOJ recommends that there be slot divestitures and carve outs in certain markets as a precondition for approval of the AA/BA alliance.

Specifically, DOJ argues that the combination of U.S.-London services of AA/BA through an immunized alliance will result in immediate competitive harm and that

divestiture of well-timed LHR [London Heathrow] slots and related facilities sufficient to permit nine new daily round trips by new entrants could substantially remedy the competitive harm in NYC-LHR and BOS-LHR. Those two markets have well-positioned new entrants that would be likely to offer service if they had sufficient slots and facilities at LHR. . . . Moreover, unless divested slots are "earmarked" for particular markets (which we recommend against as inefficient), it is likely that slots for more than nine new dailies would have to be divested if DOT is to assure that existing competition in the New York and Boston markets will be preserved.¹⁴⁷

DOJ maintains that "to achieve *de facto* Open Skies, DOT must provide for slots and related facilities in addition to those needed to remedy the competitive harm in the NYC and BOS markets."¹⁴⁸ Moreover, DOJ argues that the Department should delay the effectiveness of any immunity order until carriers that receive divested slots and facilities are in a position to begin new service to remedy competitive service in the harmed markets. DOJ suggests that the delay could involve phase-ins of immunized operations by AA/BA in certain markets and should specify certain dates rather than any performance measures by new entrants, noting that a date certain would maximize the incentive of new entrants to develop their competitive service as quickly as possible.¹⁴⁹ **Continental** agrees that divestitures must occur no later than the date antitrust immunity is granted and notes further that alliance partners must be required "to relinquish adequate facilities such as gates, ticket counters, back offices, baggage facilities and service offices, transfer desks, airport lounges, piers, office space, and storage areas in prime locations."¹⁵⁰ **Northwest** also concurs and further argues that the relief suggested by DOJ "is not only required to vindicate a true Open Skies policy by ensuring competitive entry and market structure in all relevant city pair routes affected, but is necessary 'to meet DOT's public interest standard.' . . . In other words, if securing an Open Skies agreement with the U.K. is to be the

¹⁴⁵ DOJ Comments at 3-4.

¹⁴⁶ Id. at 10-11.

¹⁴⁷ DOJ Comments at 4. Specifically DOJ recommends that at least seven daily round trips should be made available to new entrants in the New York-London Heathrow market and two daily round trips in the Boston-London Heathrow market. (DOJ Comments at 50-51.).

¹⁴⁸ Id. at 53.

¹⁴⁹ Id. at 54.

¹⁵⁰ December 17 Answer and Supplemental Comments of Continental at 27.

justification under the public interest standard for approving this otherwise patently anticompetitive alliance, then the Department must ‘in fact’ achieve true Open Skies.”¹⁵¹

In addition, DOJ states that the Department should minimize competitive harm by imposing carve-out conditions, as in past cases, for two routes with respect to AA/BA for which entry is unlikely—the Chicago-London Heathrow market and the Dallas/Fort Worth-London Heathrow market. DOJ notes that since Chicago O’Hare is a major hub for both American and United, and Heathrow is a hub for British Airways and bmi, a would-be entrant would face two incumbents with hubs at both ends should the pending applications be approved. In such circumstances, DOJ states that successful entry would be materially more difficult. Regarding Dallas/Fort Worth-Heathrow, DOJ states, “even if the alliance does not switch its DFW service to LHR in order to provide ‘beyond-beyond’ connecting opportunities, DFW-LON will connect a major alliance hub with a city with dominant alliance presence.”¹⁵² Thus, DOJ maintains, “carve-outs still offer some promise of reducing the loss of competition that determines the level of published unrestricted fares in the affected markets.”¹⁵³ **Continental** urges the Department to impose a carve-out on all fare types and on all of the current AA/BA overlap routes.¹⁵⁴

Virgin Atlantic argues that, if the Department decides to approve and immunize the proposed alliance, it should impose severe conditions in order to maintain effective competition on routes between the U.S. and the U.K. Some conditions include AA/BA making available a sufficient number of slots at Heathrow, together with related facilities such as terminal space, check-in desks, gates, aircraft parking areas, etc. to ensure that competitors are able to provide the level of service necessary to maintain effective competition; AA/BA’s granting full access to their Frequent Flyer Programs to any competitor seeking such access, on terms no less favorable than those applicable to any other participant, including BA and American; AA/BA’s making available to competitor airlines interline fares at their hub airports at rates no less favorable than those they charge each other; AA/BA’s agreeing not to pad CRS screens by displaying their connecting services more than once; BA/American’s agreeing not to abuse the dominant position they would have on U.K./U.S. routes by entering into arrangements with travel agents or corporate customers whereby sales are in any way “tied”; and replacing the Bermuda 2 bilateral agreement in order to allow new entry into Heathrow-U.S. routes.¹⁵⁵ Virgin also states “it is essential that the Department considers [screen padding] and takes steps to ensure that AA and BA cannot pad CRS screens to ensure that competing flights are pushed down the screen or indeed onto subsequent screens.”¹⁵⁶ Finally, Virgin states its view that the alliance between British Airways and American Airlines should not be granted any form of immunity from the competition laws on both sides of the Atlantic and that such an immunity cannot be legally granted. It, therefore, states that it reserves the right to take whatever action is necessary to ensure that effective competition is maintained in the U.K.-U.S. markets.

The **Houston Parties** argue that U.S. gateways that currently lack access to Heathrow, and carriers that are currently not allowed to operate their own service to Heathrow, must have meaningful access to Heathrow and that expanded access to Heathrow can be achieved by

¹⁵¹ December 21 Supplemental Reply of Northwest, at 8.

¹⁵² DOJ Comments at 45-46.

¹⁵³ Id. at 51.

¹⁵⁴ Continental December 17 Answer and Supplemental Comments at 32 and December 21 Reply at 6.

¹⁵⁵ Initial Answer of Virgin Atlantic at 146-147.

¹⁵⁶ December 17 Answer of Virgin Atlantic at 28-29.

“divestment” of slots by American and British Airways.¹⁵⁷ They urge the Department to negotiate an Open Skies agreement with the U.K. that would ensure that non-incumbent carriers have a meaningful opportunity to establish services at Heathrow from gateways that are currently deprived of such services with commercially viable slots on the same basis that U.K. carriers receive their U.S. slots, *i.e.*, at no charge; that during a transition period, AA/BA not be permitted to implement their alliance or to operate code-share services at American’s hubs and at gateways to London which are served only by American and British Airways; and that following a transition period, an immunized American/BA alliance would not be permitted to establish joint services at American’s hubs and at gateways to London which are served only by American and British Airways, unless corresponding or equal service opportunities are available for non-incumbent carriers.¹⁵⁸

The New Jersey Parties, while still advocating disapproval of the AA/BA alliance, argue that if the Department decides to permit the alliance to proceed, then “competitors of the alliance must be able to operate all the flights they deem necessary and to add flights as the market or competitive conditions demand.”¹⁵⁹

Finally, **Continental** also argues that the Department should resolve key computer reservations systems issues before completing this proceeding. Continental states that while American and British Airways have stated resolution of those issues is more appropriately addressed in the CRS rulemaking proceeding (Docket OST-97-2881), Continental maintains that the Department must resolve those issues before permitting AA/BA “to exploit their dominance in CRS listing by implementing their proposed merger on U.S.-London routes.”¹⁶⁰ In addition, Continental maintains that the Department’s procedures are inadequate to evaluate the alliances and that the applicants have not fully complied with the Department’s requirements. Continental argues that the reason the Department did not hold an oral proceeding to consider the unique facts of this case “suggests that the Department has been unduly influenced by a foreign government and its objectives, to the detriment of U.S. consumers, airlines, and cities.”¹⁶¹

C. Comments of Alliance Partners

1. AA/BA

AA/BA state that they do not oppose the antitrust application of United, bmi, Austrian, Lauda, Lufthansa and SAS, provided that the AA/BA antitrust application for immunity is contemporaneously granted. They maintain, however, that it would be contrary to the public interest for the Department to authorize an immunized alliance to United/bmi while denying the same status to AA/BA, and that United/bmi is not substantial enough to achieve Open Skies with the U.K. Thus, they agree that the two antitrust applications are linked, as neither can be achieved without Open Skies, and urge the Department to grant both promptly. AA/BA maintain that all of the benefits that United/bmi cite in support of approval of their alliance apply equally to AA/BA, including (a) the fact that the transatlantic market is very competitive and, thus, there will be a significant number of competitors to challenge the alliance; (b) linking of global networks will be facilitated; (c) approval will increase the range of competitive service options

¹⁵⁷ Initial Answer of the Houston Parties at 4-5.

¹⁵⁸ *Id.* at 8.

¹⁵⁹ December 21 Reply of the New Jersey Parties at 5.

¹⁶⁰ December 17 Answer and Supplemental Comments of Continental Airlines at 34-35.

¹⁶¹ *Id.* at 39.

and reduce fares; (d) carriers will be able to transform the level, quality, and competitiveness of the international air services that they offer; (e) alliance competition will be promoted; (f) a reduction in fares in gateway markets will be facilitated; and (g) the development of global alliances will be promoted and those global alliances, in turn, will encourage nations to liberalize their relationships with the U.S. Thus, AA/BA argue that the Department can best maximize global network competition by increasing the number of immunized alliances.¹⁶²

AA/BA further maintain that since the Star alliance has 27% of all slot holdings at Heathrow, it is well positioned “as a formidable competitor to AA/BA between the U.S. and London, as well as in behind and beyond markets on a global basis.” They further argue that tying bmi into the Star alliance makes Heathrow an integral part of a highly competitive multi-hub network, significantly boosts the competitive power of the Star alliance, and that competing alliances at Heathrow will produce significant consumer and competitive benefits, rather than reducing competition as argued by the opponents.¹⁶³ AA/BA reiterate their contention that their alliance is comparable in scope to the United/bmi alliance and that Star is even larger, thus supporting approval of the AA/BA application to promote competition.¹⁶⁴

AA/BA also contend that bmi competes vigorously with BA in beyond-Heathrow markets. They state that “while BA serves more cities in Europe from Heathrow (82 cities) than bmi (36 cities), bmi provides service to the most important markets,” which comprise 70% of the aggregate O&D traffic between the U.S. and BA’s 82 beyond-Heathrow cities.¹⁶⁵ Of the 46 cities served by BA but not by bmi, they state that all but 10 small cities are served by other Star partners and note that the 10 cities represent only 0.3% of the U.S.-Europe O&D market.¹⁶⁶ AA/BA contend that Europe’s four largest hubs are Heathrow, Frankfurt, Amsterdam and Paris, and that these four handle comparable numbers of connecting passengers between the U.S. and Europe and beyond. They maintain that once the AA/BA, United/bmi, and Delta/Air France alliances are immunized by DOT, they will compete vigorously for connecting traffic.¹⁶⁷

American further argues that it needs to rely on British Airways to “fill the network void left by Swissair and Sabena in order to effectively compete with other transatlantic alliances.” In this regard, American maintains that it is being forced to discontinue code sharing to 32 European points served by Swissair and its affiliates and that American can no longer rely upon Sabena and its affiliates for 37 points in Europe that they had served.¹⁶⁸

In addition, AA/BA argue that the Department should reject arguments by United and bmi that they will need additional Heathrow slots and facilities. In this regard, AA/BA state that bmi is the second largest holder of slots at Heathrow (approximately 14%) and the Star alliance carriers collectively hold approximately 27% of all Heathrow slots. While bmi contends that its Heathrow slots are suitable only for narrow-body operations, AA/BA note that “the British Airports Authority, . . . has stated that (assuming carriers have runway slot times) terminal and other facilities will allow as many as 10 new daily transatlantic services at Heathrow by US carriers to be accommodated in the first traffic season after open skies (winter 2002/2003), and as

¹⁶² December 17 AA/BA Joint Answer (public version) at 3-6.

¹⁶³ Id. at 8.

¹⁶⁴ Id. at 9-10.

¹⁶⁵ Id. at 11 and Exhibit JA-4.

¹⁶⁶ Id. at 11 and Exhibit JA-12.

¹⁶⁷ Id. at 12.

¹⁶⁸ Id.

many as another four in the following season (summer 2003).¹⁶⁹ Moreover, they state that United and bmi will be able to optimize use of existing facilities and redeploy them to add transatlantic service. Thus, they argue that United/bmi's arguments for transfer of slots to them is not credible.¹⁷⁰

The December 21 Reply of AA/BA primarily consists of responses to DOJ comments and Continental's procedural arguments relevant to this proceeding. AA/BA state that since the Department last looked at their alliance, AA/BA's U.S.-U.K., U.S.-London and U.S.-Heathrow market shares have declined with American's now ranking fourth among all carriers serving London and last among the four that serve Heathrow. AA/BA also maintain that their overlap markets are now more competitive, including Boston and New York. They claim to have only 6 routes that overlap and note that five of those have nonstop competition. They also claim that other factors, such as corporate contracts and increased London services by other alliances, have increased competition.¹⁷¹

AA/BA also maintain that DOJ's proposed 9-slot remedy is without justification and ignores many of their arguments and much of the factual record. They claim that the proposed 9-slot remedy is based on unsupportable evaluations of the London routes to New York and Boston and cannot be supported by an objective analysis. They argue that the "request for these additional slots is designed to achieve some ill-specified policy goals rather than curing competitive problems stemming from the alliance."¹⁷² Further, they allege that DOJ "not only has failed to acknowledge the very substantial benefits that . . . would flow from the proposed alliance and open skies, but has strayed from the competition principles it claims to uphold into obscure notions of industrial planning under the rubric of 'public policy'."¹⁷³ Moreover, they state that DOJ failed to take into consideration the impact the slot divestitures would have on the efficiency of oneworld in London and its ability to compete with other alliances.

More specifically, AA/BA contend that DOJ's concern regarding Boston and New York is unwarranted and unsubstantiated. With respect to Boston, AA/BA note that DOJ recommends the same divestiture of two round trips at Boston as it did in 1998 when only American and British Airways served Boston. AA/BA maintain that now more carriers serve the Boston market, with United and Virgin serving Heathrow and Delta serving Gatwick, as well as Continental's code-share service on Virgin's flights. They maintain that United will become stronger with an immunized alliance and argue that Delta would not serve Gatwick if it were not successful. Moreover, contrary to DOJ's claims, AA/BA argue that Virgin's service is successful with a 25% passenger share compared to only a 12.5% frequency share.¹⁷⁴ In addition, AA/BA argue that DOJ's focus on business passengers does not alter the highly competitive nature of the Boston-London route.¹⁷⁵ In sum, AA/BA argue that the remedy proposed has already been met by services that have been added to the market since 1998 and that the DOJ analysis of the Boston-London market is flawed.

¹⁶⁹ Id. at 14-15, citing BAA submission, OST 2001-10387, October 4, 2001, at 3.

¹⁷⁰ Id. at 15.

¹⁷¹ Reply at 2.

¹⁷² Id. at 5.

¹⁷³ Id.

¹⁷⁴ Id. at 6-7.

¹⁷⁵ Id. at 9.

Similarly, AA/BA maintain that the concern about the New York-London market is unwarranted and the suggested remedy unnecessary. They argue that while DOJ maintains that 3-4 daily flights (with at least one from Newark) are needed to “compete seriously” for New York passengers, DOJ (without explanation) calls for a remedy of 7 daily flights.¹⁷⁶ AA/BA state that today “five carriers serve the New York-London route with at least two frequencies each—American, British Airways, Virgin, United and Continental” and that following approval of the alliances, “there will continue to be at least four effective competitors—American/British Airways, United/bmi, Virgin and Continental.” AA/BA contend, “DOJ and opponent airlines have failed to establish a competitive concern in need of any remedy, let alone divestiture of seven frequencies.”¹⁷⁷

AA/BA contend that DOJ failed to recognize factors that obviate the likelihood of competitive harm. According to AA/BA, DOJ failed to consider properly studies entered into the record that demonstrated that AA/BA would not have an incentive to raise fares to business passengers, failed to credit the proposed alliance for enhancement of competition for corporate discount contracts, and failed to attribute any competitive significance to one-stop service on long-haul international routes.¹⁷⁸ AA/BA maintain that, contrary to DOJ’s arguments and those of the opposing parties, their alliance will be unable to impose unwarranted fare increases on business passengers, even those that do not purchase tickets through corporate discounts, and that approval of the AA/BA alliance will result in reduced fares, more convenient schedules, seamless connections, and reciprocal frequent flyer programs.¹⁷⁹

AA/BA also state that, contrary to statements by others, Gatwick is a growing and viable alternative to Heathrow for both unrestricted and restricted fare passengers. In this regard, AA/BA maintain that DOJ and other opponents failed to give proper weight to the competitive significance of Gatwick Airport. AA/BA argue that the current Bermuda 2 agreement has impeded the development of Gatwick, a situation that will be remedied by Open Skies; that all of the carriers that serve Gatwick, including American, have been restricted in the number of flights that they can operate from their hubs to Gatwick; and that there are no location or facilities disadvantages that make Gatwick an undesirable terminus for U.S.-London passengers. Moreover, they state that “historic service patterns driven by Bermuda 2 that have given Heathrow a larger share of transatlantic traffic do not justify placing Gatwick at the margins of forward-looking competitive analysis.”¹⁸⁰

AA/BA argue that DOJ incorrectly concluded that AA/BA must divest Heathrow slots.¹⁸¹ AA/BA maintain that even if one were to accept DOJ’s concern over competitive effects at Boston and New York, “divestiture is not necessary to accommodate the limited number of new transatlantic services envisioned by DOJ.” Moreover, they state that carve-outs on Chicago and Dallas/Ft. Worth are not warranted, noting that DOJ has not demonstrated that substantial harm is likely on the DFW-London route.¹⁸² They argue that proper analysis would show that Gatwick

¹⁷⁶ Id. at 11, citing pages 44 and 50 of DOJ comments.

¹⁷⁷ Id. at 11-12.

¹⁷⁸ Id. at 18-28.

¹⁷⁹ Id. at 2-3.

¹⁸⁰ Id. at 34-35. AA/BA also argue that even now Gatwick provides a competitive constraint on Heathrow, and notes that Heathrow and Gatwick are both full service airports with direct rail and road access to central London. (Id. at 35).

¹⁸¹ Id. at 44, 55.

¹⁸² Id. at 59

service constrains Heathrow prices and obviates the need for Heathrow slots and that AA/BA will by no measure have a “dominant” share of Heathrow slots. Moreover, they allege that “nearly all carriers . . . understand that slot trading among alliance partners and other airlines will provide an economically logical and viable method for obtaining Heathrow slots that can be used for transatlantic service” and that “documents produced in this proceeding by bmi belie DOJ’s conclusion that slot trading will not occur.”¹⁸³ AA/BA argue that “forced divestiture might benefit those alliances and carriers that seek to hobble AA and BA, but such unnecessary, politically motivated divestitures would serve only to injure the AA/BA network, thus hindering the ability of the AA/BA alliance to compete with other alliances, and therefore be contrary to be interests of the flying public.”¹⁸⁴

AA/BA also argue that DOJ and airline opponents improperly recommend slot remedies unrelated to any alleged competitive harm. AA/BA argue that the slot remedies have nothing to do with the competitive analysis of the alliance and that DOJ and the slot opponents seek slots for services in markets where there has not been demonstrated a competitive issue, i.e. services in non-overlap markets. AA/BA maintain that “the opponents’ self-serving, unsubstantiated claims that they will be unable to obtain slots from alliance partners are not credible, and DOJ erred in relying on such claims.”¹⁸⁵ AA/BA argue that

to the extent that any argument can be made that the public interest requires new entrants to be given access to Heathrow in connection with city-pair routes on which the AA/BA alliance will have no substantial, harmful impact on competition, such an argument would apply with equal force to all incumbents at Heathrow, including United and bmi. No justification exists for singling AA and BA out. In sum, by urging the divestiture of AA and BA slots without regard for what would be a legitimate competitive analysis of the AA/BA alliance, opponents of the alliance are seeking a government hand-out in an attempt to eviscerate the AA/BA network and gain a competitive advantage to the detriment of consumers.¹⁸⁶

Finally, AA/BA argue that Continental’s procedural arguments are without merit as they are obviously made solely for delay and that the Department should reject such tactics. Contrary to Continental’s assertion that the Department’s decision not to hold an oral hearing was “unexplained,” AA/BA argue that indeed the Department found that (citing Order 2001-12-5) “neither the statute nor our rules requires oral evidentiary hearings in alliance cases” and that “holding a formal hearing would require a significant amount of time and thereby delay our decision.”¹⁸⁷ Moreover, AA/BA maintain that Continental’s contention that the Department has been unduly influenced by a foreign government is misplaced, noting “the fact that negotiation of a U.S.-U.K. open skies agreement is linked to approval of the AA/BA alliance has been common knowledge for years. That linkage is consistent with and *required* by the long-standing U.S. policy requiring an open skies agreement as a prerequisite to alliance antitrust immunity.”¹⁸⁸ To Continental’s charge that the applicants have failed to update the record, AA/BA note that, in

¹⁸³ Id. at 45 and 52.

¹⁸⁴ Id. at 55.

¹⁸⁵ Id. at 54.

¹⁸⁶ Id. at 56.

¹⁸⁷ Id. at 68.

¹⁸⁸ Id. at 68-69.

response to the Department's Order 2001-11-10, the joint applicants have submitted voluminous material, including some 80 internal documents.¹⁸⁹

2. United/bmi

United/bmi note that no answering party offered any comments regarding the integration of the expanded United/bmi alliance into United's existing alliance with Austrian, Lufthansa and SAS. In fact, they cite DOJ's assessment that "there is no significant competitive overlap among the parties to the United/bmi transaction in any U.S. markets . . . [and] there is no reason . . . nor has DOJ or any other party offered one, for deferral of the immunity for the United/bmi expanded alliance."¹⁹⁰ Thus, United/bmi distinguish their alliance to that of AA/BA, arguing, "granting immunity to the United/bmi alliance, unlike the AA/BA alliance, poses no risk to existing (or potential) competition."¹⁹¹

United/bmi state that they oppose grant of immunity to AA/BA unless the Department imposes appropriate conditions to preserve competition on U.S.-Heathrow routes and to facilitate access to Heathrow by competitors.¹⁹² In this regard, they further distinguish their application from that of AA/BA, stating that while DOJ has recommended deferral of effectiveness of any immunity to AA/BA until carriers that receive slots and facilities are in a position to begin new service to remedy competitive harm, that same assessment should not apply to United/bmi. United/bmi maintain that they and their alliance partners "require no less of a head start in preparing for competition against a combined AA/BA than do the new US carrier entrants at Heathrow . . . [and that] immediate antitrust immunity will afford bmi and its partners the opportunity to integrate their operations at Heathrow so as to be ready to compete more effectively with American/BA once the latter alliance's immunity becomes effective."¹⁹³ Thus, United/bmi maintain that United/bmi should be allowed to implement their expanded alliance as soon as possible under a U.S.-U.K. open skies agreement, without any regard to any phasing that may be required for full effectiveness of immunity for AA/BA.

Regarding their Star Alliance, United/bmi state that "because United is the only one of the Star Alliance carriers applying for this immunity in this proceeding that currently operates direct LHR [Heathrow]-US service, and because United and bmi will be the only Star Alliance applicants positioned to operate nonstop LHR-US service under an open skies agreement, opponents' efforts at aggregating all of the Star carriers' slot holdings at LHR as a means of suggesting market concentration is entirely misplaced."¹⁹⁴

United/bmi acknowledge that opponents in this proceeding have complained about a "duopoly" effect at Heathrow. They argue, however, that the complaining carriers ignore the fact that, "with two alliance hubs operating at Heathrow, both alliances will be better able to offer important competition to the opponent's European alliance hubs at Amsterdam and Paris."¹⁹⁵

¹⁸⁹ Id. at 70.

¹⁹⁰ December 21 Consolidated Reply of United/bmi at 3, fn 2, and at 19.

¹⁹¹ Id. at 17.

¹⁹² Id. at 7.

¹⁹³ Id. at 19.

¹⁹⁴ Id. at 8, fn 5.

¹⁹⁵ Id. at 14.

Additionally, United/bmi state that the Department need not worry about a supposed “duopoly” so long as the American/BA alliance is properly conditioned as DOJ has proposed.¹⁹⁶

United/bmi state that their alliance represents the best means available to “ensure effective network-to-network competition on U.S.-LHR [Heathrow] routes.” They note, however, that only with immunity can they be in a position to develop the integrated network of services at Heathrow to provide a meaningful competitive counter-weight to the integrated network of transatlantic services that AA/BA will be able to offer.¹⁹⁷ In this regard, they state that “the ability of United to integrate fully its U.S.-LHR services with bmi’s LHR network of local U.K. and intra-European services is necessary to enable United to remain a competitive factor after BA and American effectively merge their LHR and LGW [Gatwick] operations.”¹⁹⁸

V. Statutory and Public Interest Decisional Standards

AA/BA and United/bmi have applied under 49 U.S.C. §§41308 and 41309 for approval of and antitrust immunity for Alliance Agreements, whereby they will plan and coordinate service over their respective route networks as if there had been an operational merger between the partners. Section 41309 authorizes the Department to approve agreements between U.S. and foreign airlines related to foreign air transportation, and section 41308 authorizes the Department to immunize agreements approved under section 41309 from the antitrust laws.

Section 41309 creates a three-step process for consideration of the approval of an agreement insofar as antitrust issues are involved. *Republic Airlines v. CAB*, 756 F.2d 1304, 1313-1315 (8th Cir. 1985). The Department must first determine under antitrust law standards whether the agreement will eliminate or substantially reduce competition. If not, the Department must approve it if the agreement is not adverse to the public interest. If the agreement would eliminate or substantially reduce competition, the Department must consider whether the agreement is necessary to meet a serious transportation need or secure important public benefits, including international comity or foreign policy considerations. 49 U.S.C. §§41309(b)(1). If the agreement is not necessary to meet a serious transportation need or secure important public benefits, the Department must disapprove it. If the agreement, on the other hand, is necessary to meet a serious transportation need or secure important public benefits, the Department must consider whether that need can be met, or those benefits secured, through reasonably available alternative means that are materially less anticompetitive. If there are no reasonably available alternative means for meeting that need, or securing those benefits, that would be materially less anticompetitive, the Department must approve the agreement.

Under section 41309, the party opposing the agreement or request has the burden of proving that it substantially reduces or eliminates competition and that less anticompetitive alternatives are available. On the other hand, the party defending the agreement or request has the burden of proving the transportation need or public benefits.

In addition, as noted, we may not approve an agreement that is adverse to the public interest.

¹⁹⁶ Id. at 13.

¹⁹⁷ Id. at 11.

¹⁹⁸ Id. at 14.

Section 41308 gives the Department the discretion to exempt a person affected by an agreement approved under Section 41309 from the operation of the antitrust laws “to the extent necessary to allow the person to proceed with the transaction,” provided that the Department determines that the exemption is required in the public interest. It is not our policy to confer antitrust immunity simply on the ground that an agreement does not violate the antitrust laws. We are willing to make exceptions, however, and thus grant immunity, if the parties to such an agreement would not otherwise go forward without it, and we find that the public interest requires that we grant antitrust immunity.¹⁹⁹

Since AA/BA and UA/bmi both propose arrangements that are intended to create a framework that will allow them to cooperate so the airlines can create a seamless air transport system, the Alliance Agreements’ intended commercial and business effects are equivalent to those resulting from a merger of applicants. In determining whether the proposed transaction would violate the antitrust laws, we apply the Clayton Act test used in examining whether mergers will substantially reduce competition in any relevant market.²⁰⁰

The Clayton Act test requires the Department to consider whether the Alliance Agreements will substantially reduce competition by eliminating actual or potential competition among the Joint Applicants so that they would be able to produce supra-competitive pricing or reduce service below competitive levels.²⁰¹ To determine whether a transaction is likely to violate the Clayton Act, the Department considers whether the transaction is likely to create or enhance market power, market power being defined as the ability profitably to maintain prices above competitive levels or to reduce product and service quality below competitive levels for a significant period of time. To determine whether a proposed transaction is likely to create or enhance market power, we primarily consider whether the transaction would significantly increase concentration in the relevant markets, whether the transaction raises concern about potential competitive effects in light of concentration in the market and other factors, and whether entry into the market would be timely, likely, and sufficient either to deter or to counteract a proposed transaction’s potential for harm.

In determining whether the proposed alliances satisfy the statutory public interest standard, we are following our longstanding policy that no alliance between a U.S. airline and a foreign airline will be approved and given antitrust immunity unless the United States has an Open Skies agreement with the foreign airline’s homeland. The existing aviation services agreement between the United States and the United Kingdom bars any U.S. airline except American and United from serving Heathrow, the London airport preferred by a large number of travellers, especially business travellers. We have therefore stated that we would not approve and immunize an alliance agreement between American and British Airways without *de facto* Open Skies: “*de facto* Open Skies in the case of the United Kingdom must include adequate provision for new and expanded U.S. carrier service through London airports, particularly Heathrow, and the ability of U.S. carriers to provide such service notwithstanding the constraints at Heathrow would be a critical consideration in our evaluation” *Joint Application of American Airlines and British Airways*, Order 99-7-22 (July 30, 1999) at 2.

¹⁹⁹ See, e.g., Order 97-6-30 at 15.

²⁰⁰ Order 92-11-27, at 13.

²⁰¹ Id.

VI. Tentative Decision on AA/BA Alliance

A. Summary of Decision

In reviewing the AA/BA alliance proposal, we will follow the three-step process established by section 41309. We will first consider whether the alliance would eliminate or substantially reduce competition in any market and, if so, whether conditions may be imposed that would prevent that competitive harm. We will then consider whether the alliance would provide public benefits or meet transportation needs that cannot be obtained by reasonably available alternatives that would be substantially less anticompetitive. Our public benefit analysis will also examine whether the alliance as conditioned would be adverse to the public interest.

We have tentatively concluded, as explained below, that the alliance, subject to our proposed conditions, will satisfy the statutory antitrust and public interest tests. Our conditions will require AA/BA and UA/bmi to divest sufficient slots to enable other airlines to replace the competition lost in two of the overlap city-pair markets, New York City/Boston-Heathrow. We are tentatively requiring AA/BA to divest additional slots to ensure that *de facto* Open Skies will exist at Heathrow. Without those additional slot divestitures, the alliance would be adverse to the public interest, since it would freeze in place the existing unsatisfactory situation at Heathrow. Under Bermuda 2 only two U.S. airlines – AA and United – have been allowed to serve Heathrow. While a new Open Skies agreement would eliminate bilateral entry-barriers, it would not eliminate all barriers to competition in the U.S.-U.K. markets. Entry into Heathrow airport is constrained by landing and take-off limitations (“slots”) and by facility limitations. The evidence before us indicates that it will be difficult for other carriers to obtain slots and facilities to begin or expand U.S.-Heathrow service in the short run, either through the slot allocation process or from code share/alliance partners, without divestiture.

As a result of our analysis, we have tentatively decided to approve and grant immunity to the proposed AA/BA alliance subject to the following conditions:

1. We will require AA/BA to provide other U.S. airlines with useable slots and facilities at London’s Heathrow Airport for 16 daily roundtrips. For reasons that will be discussed below, we have tentatively concluded that these slots and facilities should be allocated as follows: 5 for Continental, 6 for Delta, 3 for Northwest and 2 for USAirways.
2. We will limit the grant of immunity so that it takes effect only when the new entrants have the full opportunity to use the slots and facilities that we are requiring AA/BA to provide them.
3. We will also limit our grant of immunity so that it does not extend to pricing, inventory or yield management coordination, or pooling of revenues, with respect to unrestricted coach-class fares or any business or first-class fares for local U.S.-point-of-sale passengers flying nonstop in certain markets. The purpose of this condition is to prevent the AA/BA alliance from exercising market power with respect to time-sensitive travel. The markets covered by this so-called “carve-out” condition are the Chicago-Heathrow and Dallas/Ft. Worth-Gatwick/Heathrow markets.

4. We will also require AA/BA to submit their alliance agreements for review in three years, rather than in five years, as we require in most other alliance cases. This requirement will enhance our ability to monitor the results of our decision in this case.

We have also tentatively decided to approve and grant immunity to the proposed UA/bmi alliance subject to the condition that bmi provide a useable slot and facilities at London's Heathrow Airport for one new daily service by United in the Boston-Heathrow market.

In addition, consistent with our long-standing policy, we shall require that there be an Open Skies agreement with the United Kingdom in place before we issue a final decision in this proceeding. The immunity would take effect only when competitors have the full opportunity to use the 17 divested slots.

Our proposed conditional approval of the AA/BA and UA/bmi alliances will provide significant public benefits. Our decision may enable us to obtain for the traveling public the benefits of an Open Skies agreement with the United Kingdom. One of the most important U.S. aviation policy objectives is the elimination of restrictions on airline operations in international aviation markets. The United States relies heavily on Open Skies regimes with no regulatory constraints on pricing and entry to achieve this objective. Our proposed decision would facilitate the opportunity for four U.S. airlines to enter the U.S.-Heathrow market with new freedoms to operate and price their services in response to consumer demand. These four carriers' new services will enable consumers to receive more than 5800 nonstop roundtrips annually from the selected U.S. gateways. Since it is likely that the new nonstop services will operate from gateway points that are also airline hubs, the new entrants will be able to use their extensive domestic route systems to provide an even larger number of consumers with new or improved on-line service. Our proposed action will also benefit the public interest, enhancing the competitive position of U.S. cargo airlines in international aviation markets, and enhance the ability of the United States to negotiate an Open Skies agreement with the European Union.

In light of all of the circumstances, and after careful consideration of all of the evidence and pleadings in this case, we tentatively find and conclude (1) that the transaction, as conditioned, would not substantially reduce competition, (2) that even if it did, our proposed action is necessary to secure important public benefits that would not be otherwise obtainable, and (3) that it will not be adverse to the public interest.

B. Competition Analysis

Our first step in reviewing the alliance, as required by the statute, is to determine whether the alliance would eliminate or substantially reduce competition in any market. In undertaking that analysis, we will follow the Clayton Act standards applied in merger cases. The alliance proposals presented in this case affect many more travellers than those we have considered in earlier international alliance cases, due to the large size of the U.S.-London markets affected by the proposals. The proposed alliance between AA and BA particularly raises more serious and complex issues than those we have considered before, both because of the degree of overlap between the two applicants' services, the size of the overlap markets, and the difficulty of entry at the key airports at issue, Heathrow and Gatwick. In this particular case, we have found the detailed factual analysis and investigation conducted by the Justice Department to be very helpful. Our tentative conclusions on those issues agree with the Justice Department's recommendations on the issues of market definition (the issue of whether separate markets exist

for time-sensitive travellers with a strong preference for Heathrow service) and the inability of other airlines to enter Heathrow easily and on almost all of the remedies recommended by the Justice Department for the potential loss of competition created by the AA/BA alliance. We have largely accepted the Justice Department's recommendations regarding actions needed to correct the competitive problems.

The starting point for our competitive analysis is to identify the relevant markets that would be affected by the implementation of the proposed alliance. We have tentatively determined that the relevant markets in this case are (1) U.S.-Europe, (2) U.S.-U.K., (3) U.S.-London nonstop city-pair markets, and (4) regarding the latter, U.S.-Heathrow markets.

We have analyzed the alliance's potential competitive impact in light of the traffic and service levels that existed before the terrorist attacks of September 11. We recognize that those attacks have led to substantial declines in transatlantic traffic levels and the number of flights on U.S.-U.K. routes. We assume, however, that traffic and capacity will return to previous levels over the next several years. This tentative finding is consistent with the Justice Department's recommendation on this issue.²⁰²

C. The Relevant Markets

1. U.S.-Europe

The U.S.-Europe market is now highly competitive. Six U.S. airlines provide scheduled passenger service in this market from their hubs, either individually or in conjunction with an existing alliance. This market is also served by more than forty foreign airlines, principally from their hubs.

We have tentatively determined that the U.S.-Europe market will remain competitive if the AA/BA alliance is approved. The oneworld alliance would have a larger share of the transatlantic market than any other alliance, with 26 percent of the scheduled passenger traffic between the U.S. and European gateways. However, the Star Alliance has a 20 percent share, the SkyTeam Alliance has a 17 percent share,²⁰³ the Northwest/KLM Alliance has a 9 percent share, and Continental, Virgin Atlantic and US Airways have 6, 7, and 3 percent shares, respectively.²⁰⁴ The evidence in this proceeding supports a tentative finding that these alliances and airlines will provide effective competitive options for the services proposed by AA/BA.

In reaching this conclusion, we have given material weight to the presence of the Star, SkyTeam and Northwest/KLM alliances in the U.S.-Europe market and their ability to offer attractive alternatives to the AA/BA alliance. Consequently, we are prepared to reexamine our approval of the proposed AA/BA alliance should there be a significant change in market conditions affecting alliance competition in this market.

²⁰² DOJ Comments at 7.

²⁰³ The Star Alliance members include United, Lufthansa, SAS, Austrian, Singapore Airlines, Air New Zealand, and Lauda. The SkyTeam members include Delta, Air France, CSA Czech Airlines, and Alitalia.

²⁰⁴ T-100 and T-100f data for Calendar Year 2000.

2. The U.S.- U.K. Markets

Our analysis of the U.S.-U.K. markets will focus on the U.S.-London markets, since there is no overlap between the applicants' service between U.S. points and British points other than London. Nothing in the record indicates that other U.S. airlines would be unable to begin (or increase) service to points such as Manchester or Glasgow if AA/BA increased fares above competitive levels.

More than 90 percent of all U.S.-U.K. travelers use London as their gateway to the U.K.²⁰⁵ Six U.S. carriers and 2 U.K. carriers serve the U.S.-London market: American, Continental, Delta, United, Northwest, US Airways, British Airways and Virgin Atlantic.

As noted, Bermuda 2 permits only American, United, British Airways and Virgin Atlantic to serve Heathrow. Continental, Delta, Northwest, and US Airways can only serve Gatwick with their own aircraft under the restrictions on entry imposed by that aviation agreement. British Airways is the largest carrier in the market, with 38 percent share of traffic, based on calendar year 2000 traffic data. Virgin Atlantic has a 20 percent share, American has a 13 percent share, and United has a 12 percent share. Continental, Delta, Northwest and USAirways have a combined share of 12 percent.²⁰⁶

In the summer, 2001, British Airways provided daily nonstop service to London from 21 U.S. airports. It served Heathrow from 11 U.S. airports with a total of 26 daily frequencies. In the summer, 2001, American provided daily nonstop service to London from 9 U.S. airports. It served Heathrow from 6 U.S. airports with a total of 16 daily frequencies.

AA and BA now provide competing nonstop service in the Dallas/Ft. Worth-Gatwick market and in five U.S.-Heathrow markets: Boston, Chicago, Los Angeles, Miami, and New York. United provides competitive nonstop service in the Boston, Chicago, Los Angeles, and New York markets. Virgin Atlantic provides competitive nonstop service in all of these markets except Chicago, plus Miami. No airline other than the applicants provides nonstop service in the Dallas market.

More than 5.6 million passengers -- 50 percent of all U.S.-London passengers -- traveled in the AA/BA overlap markets in calendar year 2000.²⁰⁷

Table 1 summarizes traffic and nonstop service in the Heathrow overlap markets and the Gatwick-DFW market before implementation of AA/BA.

²⁰⁵ Id.

²⁰⁶ Id.

²⁰⁷ Sources: The Department's Origin & Destination Survey of Airline Passenger Traffic, adjusted to reflect information filed in the record of this case by American and British Airways, plus estimates for Virgin Atlantic for Calendar Year 2000; and *Official Airline Guide* for July 2001.

TABLE 1²⁰⁸

MARKET		TRAFFIC NONSTOP SERVICE SUMMER 2001			
HEATHROW	O&D Pax CY 2000	AA	BA	AA& BA	OTHER
NEW YORK JFK	2,638,781	6	7	13	7 UA-3 VS-3 AI-1
EWR		1	2	3	2 UA-1 VS-1
BOSTON	765,605	2	3	5	1 UA-1 VS-1*
CHICAGO	552,605	5	2	7	4 UA-3 VS-1*
MIAMI	561,190	1	2	3	0
LOS ANGELES	873,710	1	2	3	5 UA-2 VS-2 NZ-1
* Subsequent to September 11, Virgin Atlantic moved a Heathrow service from Chicago to Boston.					
GATWICK- DFW	237,234	2	1	3	0

3. The U.S.-Heathrow Market

A key issue in this proceeding is whether the relevant U.S.-London markets include submarkets involving service to Heathrow. If Gatwick service were considered by most consumers a substitute for Heathrow service, we would not need to examine whether airlines competing with AA and BA could obtain slots and other facilities at Heathrow, if they could obtain them at Gatwick, since Gatwick flights would discipline the fares and quality of service offered on flights to Heathrow. The record demonstrates that Heathrow routes in fact constitute separate submarkets, as argued by the Justice Department.

When we had the authority under section 408 of the Federal Aviation Act, then codified as 49 U.S.C. 1378, to approve airline mergers and acquisitions, we considered in some cases whether airport-pairs constituted separate markets. We stated that, in making such a determination, "The key question in deciding whether services are in the same market is whether (and to what extent) the prices for one service respond to changes in prices in the other service." *Texas Air-Eastern Acquisition Case*, Order 86-7-21 (July 9, 1986), at 14. As we explained, "A specific airport will nonetheless constitute a separate market if there is a large number of travellers who will rarely

²⁰⁸ Id.

consider using alternative airports and, importantly, if the carriers serving that airport can disregard the level of fares and service offered at other airports in determining their fares and service levels.” *Id.* at 13. See also *Southwest-Muse Acquisition Show-Cause Proceeding*, Order 85-5-28 (May 3, 1985).

The question in the *Texas Air-Eastern* case was whether Eastern’s shuttle services between Washington National (now Reagan Washington National (DCA)) and New York City’s LaGuardia (LGA) and between LaGuardia and Boston constituted relevant markets. We noted, among other things, that most of the travellers in the shuttle routes were business travellers, that a large number of them did not consider the other Washington, D.C. and New York City airports as alternatives to Washington National and LaGuardia, that business travellers considered DCA and LGA more convenient than the other airports in the metropolitan areas, and that a large majority of them preferred to use DCA and LGA. Indeed, 80 percent of Washington-New York City business travellers used flights from Washington National. We concluded that they formed separate markets: “[T]he record indicates that fares for the DCA-LGA and LGA-BOS routes are not affected by the fares offered at IAD [Washington Dulles] or EWR [Newark], and this indicates that the shuttle markets are separate markets.” We therefore concluded that “Eastern may have the ability to maintain higher fares for business travellers unwilling to use alternative airports, a factor which supports the conclusion that the shuttle routes are submarkets.”²⁰⁹

In the *Southwest-Muse* case, on the other hand, the record showed that fares at Dallas’ Love Field and Houston’s Hobby were close to the fares offered at Dallas/Ft. Worth International (DFW) and Houston Intercontinental. Travellers from Houston and Dallas did not have a strong preference, respectively, for Hobby and Love Field.²¹⁰

Here, as in the *Texas Air-Eastern* case, the record demonstrates that a specific airport is a separate market. Indeed the factual situation here is quite similar to that presented in the *Texas Air-Eastern* case, since we are once again examining the strong preferences of business travellers to use one airport rather than another. We therefore agree with the Justice Department that the relevant markets for our antitrust analysis include the Heathrow markets, not just the markets for service between individual U.S. cities and London.

The evidence demonstrating that Heathrow is a separate market for so-called time-sensitive passengers, primarily business travelers, is compelling. It shows that:

1. Carriers that can choose between serving Heathrow or Gatwick consistently choose Heathrow for serving the United States. This consideration has helped spark airline opposition to the proposed AA/BA alliance and the related demand for fair access to Heathrow. As Northwest points out, if Gatwick were a true substitute for Heathrow, airlines would expand their operations there, and slot values at Heathrow would fall. NW Answer at 3.
2. Average round-trip fares between the U.S. and Heathrow are 31 percent higher than the average round trip fares to Gatwick, reflecting that service to Heathrow draws from a better mix of business traffic relative to discretionary traffic than does Gatwick. See Exhibit NW-8.

²⁰⁹ Order 86-7-21 at 14.

²¹⁰ Order 85-5-28 at 7-9.

3. The business traveler's preference for Heathrow is so strong that nearly 24% of U.S. carrier O&D passengers from Gatwick gateways use connecting service to Heathrow rather than nonstop service to Gatwick. These facts strongly suggest that Gatwick is not an effective substitute for Heathrow for many business passengers.²¹¹
4. Justice's analysis shows that, in the three overlap markets where premium passengers have some choice between Heathrow and Gatwick, the vast majority of those passengers [86 percent] choose Heathrow. DOJ Comments at 23 and 24. And while the joint applicants maintain that Justice's analysis is overstated because it does not include certain time-sensitive passengers, their own analysis shows that most premium passengers in these markets choose Heathrow. AA/BA Joint Reply at 37 and 38.
5. Justice's analysis also shows that American has had difficulty maintaining services to both Heathrow and Gatwick because of the Heathrow preference. Between June 1998 and October 1999, American operated Boston-Heathrow and Boston-Gatwick services. American discontinued its Boston-Gatwick service due to poor profitability. Between May 1998 and April 1999, American also operated Miami-Heathrow and Miami-Gatwick services. American discontinued its Miami-Gatwick service because of poor profitability. DOJ Comments at 20-21; *See also* Exhibit DOJ-6 Confidential.
6. Virgin Atlantic has also provided information for this record that supports the conclusion that Heathrow is a separate product market for time-sensitive passengers. In its answer to the AA/BA application, Virgin Atlantic describes its experience in serving the same U.S. city from both Heathrow and Gatwick. It notes that average yields and traffic levels are higher at Heathrow. Until recently, Virgin operated service to Newark from both Heathrow and Gatwick, and with respect to its experience in operating to both, Virgin states:

[D]espite the fact that both services were operated on a daily basis with Boeing 747 aircraft, the Heathrow service outperformed the Gatwick service in every category. Although passenger numbers on the Heathrow service were only approximately 6% higher than those on the Gatwick service, revenues were over 50% higher. An average yield improvement of 44% in an industry characterized by relatively low operating ratios is clearly significant and explains why given the choice any airline would operate from Heathrow rather than Gatwick. The principal explanation for the higher average yield at Heathrow is the fact that the airport attracts a greater proportion of time-sensitive travelers than Gatwick does. (*Footnote: This is reflected in the configurations of the aircraft on these services: the Heathrow service has 48 Upper Class seats, while the Gatwick service has 28 Upper Class seats (and seat factors average 60%.)*)²¹²

Referring to British Airways' strategy to reduce long-haul services from Gatwick, Virgin states:

²¹¹ *See* AA 0201385 Confidential and BA Network Planning Route Hub Change Proposal, BA 0006143 Confidential.

²¹² Virgin Atlantic Answer at 35-36.

British Airways' actions are yet another chapter in the long history of failed attempts by UK airlines to compete from Gatwick with services operated from Heathrow: Laker Airways, British Caledonian and Dan-Air all failed and eventually collapsed (British Caledonian was taken over by BA in 1987). This was in spite of frequently offering significantly lower published fares than competing services operated from Heathrow, including fares used by time-sensitive passengers. Virgin Atlantic has found it equally difficult to compete with its competitors' Heathrow services to Miami and Toronto operating from Gatwick.²¹³

In their Joint Reply, American Airlines and British Airways argue that the DOJ dismisses the U.K. Competition Commission's British Airways/City Flyer (1999) decision "which expressly held that 'services to common destinations from Gatwick and Heathrow operate in the same market' for business travelers."²¹⁴

We agree with Justice that that decision does not prove that Heathrow and Gatwick are in the same product market for all U.S.-London passengers. The decision examined a merger between British Airways (at Heathrow, Gatwick and other London airports) and CityFlyer (at Gatwick only). The issue, therefore, was competition at Gatwick. The U.K. Competition Commission looked at Heathrow as a substitute for Gatwick, and did find that BA at Gatwick faces competition from airlines operating at other London airports, including Heathrow. We, along with Justice, however, have examined this issue from a perspective that is more material to this case: whether and to what extent Gatwick is a substitute for Heathrow. Thus, while evidence suggests that Heathrow is an effective substitute for LGW, it does not support a finding that the reverse is true for time-sensitive passengers.

Quoting from Dr. Alfred Kahn, the joint applicants also argue that higher fares at Heathrow "is in the nature of economic rent, reflecting scarcity value, rather than monopoly profit."²¹⁵ Were the two airports in the same product market, however, passengers would switch to Gatwick rather than pay higher fares to Heathrow. In this regard, we note that from interior U.S. cities served by American to both Gatwick and Heathrow, American's fares to Heathrow are consistently and substantially higher.²¹⁶

AA/BA argue that Gatwick offers substantial advantages for travellers to London and that travellers should reasonably consider flights to Gatwick as a fully adequate substitute for flights to Heathrow.²¹⁷ This argument by AA/BA misses the point, however -- in determining whether two products or services are in the same market or in separate markets, we do not independently decide whether consumers should consider the products or services as substitutes. We instead examine whether consumers in fact consider them to be substitutes. Whether a firm dominating a market for a product or service can charge supracompetitive prices for the product or service depends on whether consumers will respond to the price increases by buying an alternative product or service -- if enough consumers will not do so despite the higher price, there is a relevant market for antitrust analysis that does not include the potential substitutes, even if consumers arguably should switch to them. When, as here, a large proportion of travellers

²¹³ Id. at 37.

²¹⁴ Joint Reply of AA/BA at 42-43.

²¹⁵ Joint Reply of AA/BA at 35, n.24.

²¹⁶ The Department's Origin & Destination Survey of Airline Passenger Traffic for Calendar Year 2000.

²¹⁷ Joint Reply of AA/BA at 34-36.

clearly do not consider one airport as a substitute for their preferred airport, any belief by us that they should do so is irrelevant.

Against this background, we have tentatively concluded that the record in the proceeding provides clear and convincing evidence that Heathrow is a separate market.

4. Nonstop Markets for Time-Sensitive Passengers

A related market definition question is whether there is a separate market for nonstop service for time-sensitive travellers, as argued by the Justice Department. After analyzing this issue, we conclude that an airline that offers all or most of the nonstop service in a U.S.-London market could profitably raise its fares by a significant amount because many time-sensitive passengers will not switch to connecting services. We recognize, of course, that many travellers, especially leisure travellers, will switch to connecting services if the airline offering nonstop service charges higher fares.²¹⁸ Many travellers, especially business travellers paying the highest fares, will not do so. As the Justice Department summarizes its evidence, passengers paying the highest fares overwhelmingly choose nonstop service, corporate travel policies allow employees to pay more for nonstop service because businesses value their employees' time and convenience, and airlines can use fare restrictions and conditions to target these time-sensitive passengers. DOJ Comments at 12. The premium traffic in U.S.-London markets rarely uses connecting services when nonstop service is available (no airline operates nonstop service to Heathrow in the one exception, the DFW-London market, so the willingness of travellers paying premium fares to use connecting flights in that market undoubtedly reflects their desire to use Heathrow, not a willingness to use connecting services when nonstop flights are available in the same airport pair). DOJ Comments at 14. The Justice Department's investigation indicates, moreover, that most business firms will not compel their employees to use connecting flights when nonstop flights are available unless the connecting service is substantially cheaper than the nonstop service. DOJ Comments at 15-17.

We find unpersuasive the arguments by AA/BA that the existence of competing connecting services would keep them from profitably imposing a fare increase for time-sensitive business travellers on nonstop flights. For example, AA/BA misinterpret the American Express survey when they imply that it shows that many corporations require employees to use connecting flights when the fare is lower than the nonstop fare.²¹⁹ In fact, however, the survey only shows that those corporations will require the use of the connecting flights when the fare is lower by some significant amount than the nonstop fare. AA/BA similarly err in claiming that they cannot charge time-sensitive passengers higher fares because those travellers will take advantage of the lower fares used by other travellers. All airlines including AA/BA have developed sophisticated revenue-management programs that allow them to charge different travellers different fares depending on their relative willingness to choose alternative service or alternative means of transportation (or not fly at all). The airlines have been able to charge non-discretionary travellers higher fares by imposing such conditions as advance-purchase requirements and Saturday-night stay requirements on passengers using discount fares. We think that AA/BA could profitably increase the fares paid by time-sensitive travelers if we did not require slot divestitures.

²¹⁸ See, e.g., Order 2001-12-18 at 15.

²¹⁹ Joint Reply of AA/BA at 29.

D. Increased Concentration From Proposed AA/BA Alliance

We tentatively find that the proposed AA/BA alliance would substantially increase concentration in four of their nonstop overlap markets, London-Boston/Chicago/New York City/Dallas-Fort Worth.

As indicated in Table 1, American and British Airways are major competitors in the Boston/Chicago/Miami/New York/Los Angeles-Heathrow and Dallas/Ft. Worth-Gatwick markets. No other airline operates more nonstop service in competition with British Airways in any of these markets than American, except at Los Angeles.

The proposed AA/BA alliance would eliminate that competition. It would also significantly increase concentration and provide the new partnership with a dominant position in markets serving a total of more than 5 million passengers annually. As shown in Table 1, the AA/BA shares of nonstop frequencies would be more than 60 percent in all of the overlap markets, except for Los Angeles.

E. New Entry

As the Justice Department explains, substantial increases in concentration in a market will lead to reduced competition, either because the combined firms have market power – the power to set prices above competitive levels – or because the combined firms and the remaining firms in the market will find it possible to tacitly coordinate their fare and service levels.²²⁰ Increased concentration will not have that result, however, if other firms can enter the market. Thus the key question in this proceeding is whether other airlines can enter the relevant markets, the nonstop U.S.-London overlap markets where the alliance will reduce or eliminate competition.

A U.S.-U.K. Open Skies agreement would create new opportunities for U.S. carriers to enter the U.S.-London markets by eliminating the restrictions on new entry imposed by Bermuda 2. However, U.S. airlines will be unable to enter Heathrow on any significant scale, since slots and other facilities at Heathrow are difficult to obtain for any airline, whether an incumbent or new entrant at the airport. *See* Exhibits DL 51, DL 52 and NW 25. In addition, AA/BA have hubs at each end of two of the overlap markets – Chicago/DFW-London – and their advantages as the hubbing airline will likely deter any other airline from entering those markets.

Entry at Heathrow is difficult, because worldwide airline demand for access to Heathrow greatly exceeds the ability of Heathrow's runways to handle the number of flights that airlines would like to provide. This situation has required authorities to allocate, or ration, arrival and departure times, known as slots. The European Union has established rules for the administration of those slots. Airport Coordination Ltd (ACL) administers those rules as the slot coordinator for Heathrow and Gatwick.

Aircraft stands, gates, and terminal capacity are also in short supply at Heathrow, particularly facilities for large aircraft during peak periods. Response of BAA, at 4. As noted by BAA, a U.S.-U.K. Open Skies agreement would exacerbate the shortage because it would produce an increase in "the proportion of long-haul services and therefore an increase in the proportion of

²²⁰ DOJ Comments at 26-30.

services with large aircraft.” BAA Issues and Principles, at paragraph 15. In the judgment of BAA, Heathrow’s terminal and parking stand capacity would permit between six and ten daily services operated by U.S. airlines in the first season of implementation, which it assumed would be the Winter of 2002/2003 season, even if those airlines could obtain slots. BAA has also stated that “Achieving the upper end of this six-to-ten range is dependent on the willingness of these new US airlines to accept retimed slots up to one hour away from their current Gatwick times and may take more than one scheduling season to achieve.” Response of BAA, at 3. It is also clear that the shortage of facilities at Heathrow will continue into the near future. BAA estimates that the construction of a new Terminal 5 at Heathrow will not be completed until 2007. Response of BAA, at 8.

There is also an important link between slots and facilities at Heathrow: in order to operate a new service on a new runway slot, an airline requires a stand, terminal space, and other terminal facilities. An airline will not be granted a slot at Heathrow unless it can operate within the terminal and aircraft parking capacity restraints. Moreover, an airline receiving slots does not gain rights to specific gate facilities: “these must be negotiated with the handler or airport operator and in some cases can take many months to be provided.” Response of BAA, at 2.

With these considerations in mind, the record in this proceeding clearly establishes that slot and facility constraints raise significant barriers to new Heathrow entry. The existence of these barriers is material to the outcome of this case because they would prevent U.S. carriers from using opportunities created by a new U.S.-U.K. Open-Skies agreement to enter Heathrow to mount an effective competitive challenge to the services proposed by AA/BA.

This conclusion is supported by substantial evidence of record, including information and analysis provided by Justice, by ACL, BAA, and, indeed, by confidential information provided by British Airways for this record.

In this regard, ACL has stated on the record in this proceeding:

In ACL’s professional judgment, the opportunities to accommodate new entrant US carriers from the allocation of pool slots in the first two seasons are extremely limited.

It may be possible to accommodate up to one daily service at timings similar to Continental’s daylight Newark-Gatwick service, with arrivals in the late evening and departures mid-afternoon the next day.

There is also scope to offer 1-2 morning rotations (ie, pairs of arrival and departure slots) on some days of on [sic] the week, principally the weekends. However, in ACL’s experience new entrant US carriers are unlikely to be willing to operate on a less than daily basis. Response of ACL, at 5

The BAA has also expressed similar views on the scarcity of slots for new entrant U.S. carrier operations at Heathrow:

BAA expects only a few additional slots to be created at Heathrow, a small amount of which are expected in the hours that transatlantic flights are currently being operated. In addition, the new slots are likely to be departure slots and are unlikely to have

accompanying arrival slots which would be required to make new services viable.
Response of BAA, at 8

DOJ and all of the airline opponents of this transaction have presented convincing evidence and analysis to support this conclusion. However, AA/BA take the position that entry barriers would not inhibit U.S. carrier entry at Heathrow because slots and facilities are available from other sources, including U.S. joint venture partners that currently serve Heathrow, and through slot trading. The record does not support the AA/BA position.

The AA/BA contention that U.S. carriers can obtain the slots needed to effectively enter the U.S.-Heathrow market from their joint venture partners rests on the joint applicants' prediction about what one or more of their competitors are likely to do. However, AA/BA have not presented probative evidence to support their claim that U.S. joint venture partners are willing to transfer slots they now use to compete with U.K. and other EU carriers on other routes to the transatlantic market, and we can find nothing in the record to support it. See Northwest Answer at pp.32-33. As argued by several parties, some U.S. airlines (USAirways, for example) do not have an alliance partner with slots at Heathrow, the foreign airlines in alliances with U.S. airlines will have incentives to continue using their slots for service to major cities in their homelands, and few foreign airlines have available slots at times that could be used for competitive transatlantic service.²²¹

Slot trading is permitted under European Rules, and sometimes involves "one carrier trading a low-value slot (which may have been obtained solely for the purpose of making a trade) plus cash for a more valuable slot." DOJ Comments, at 37. ACL has stated that while it is difficult to quantify the extent to which carriers have increased their slot holdings through slot trading, "it is ACL's observation that there is general unwillingness on the part of incumbent Heathrow carriers to divest of slots and the market is illiquid."²²² DOJ has also concluded that it is difficult to purchase Heathrow slots, particularly at peak times.²²³

Our analysis of the record, including, in particular, the confidential information submitted by AA/BA, supports the conclusion that slot trading does not materially reduce the barriers to entry in the case because it would be virtually impossible for U.S. carriers to purchase the number and quality of slots needed to compete effectively in the short run.

Nonetheless, our analysis of the evidence in this record also indicates that slot trading and the normal operation of the slot allocation process could provide U.S. carriers with some opportunity to increase their slot holdings slowly once they have effectively entered the market. In this regard, ACL and BAA point out that slot trades do occur at Heathrow, and BAA further notes that it would "expect those US carriers wishing to set up operations from Heathrow to be able to obtain at least some slots through one form of slot 'trading' or another."²²⁴

F. Need for Competitive Remedies

We tentatively conclude that our approval of the alliance must be conditioned on the divestiture of Heathrow slots and facilities for use by Continental and Delta at New York City and Boston to

²²¹ See, e.g., DOJ Comments at 38-42.

²²² Response of ACL at 5.

²²³ DOJ Comments at 38-42.

²²⁴ Response of BAA at 3.

offset the reduction in competition in the New York City/Boston-Heathrow markets that would otherwise result from the alliance (as discussed below, additional divestitures are necessary to enable us to find that the alliance will not be adverse to the public interest and that it will provide public benefits that outweigh its potential reduction in competition). We also conclude that our approval and immunity must exclude the applicants' fares for time-sensitive travellers in the Chicago/DFW-London Heathrow and DFW- London Gatwick markets.

We see no need to impose conditions protecting competition in two of the overlap markets, Los Angeles/Miami-Heathrow. As to Miami, bmi appears likely to begin service between Miami and Heathrow, as alleged by the Justice Department. The likelihood of bmi's entry means that the alliance should not cause a significant reduction of competition in that market. We also agree with the Justice Department that the alliance is unlikely to cause substantial competitive harm in the nonstop Los Angeles-Heathrow market, even though no other U.S. airline seems poised to enter this market. In contrast to the other Heathrow overlap markets and the DFW-London Gatwick market, AA/BA operate fewer than half of the frequencies on the Los Angeles-Heathrow route and carry less than half of the premium traffic. DOJ comments at 32-33.

In two of the overlap markets – Chicago- Heathrow and DFW-London – no entry is likely, because American has a hub at the U.S. gateway and BA has a hub at London.²²⁵ United, of course, also has a hub at Chicago, but it is already in the market. United's alliance with bmi may cause bmi to operate flights to Chicago, but that same alliance means that bmi cannot be treated as a new entrant that would compete with all of the incumbent firms in the market.

Since new entry in these latter two markets is unlikely, we believe that the only effective way to respond to the lost competition that would otherwise result from implementation of the AA/BA alliance is to maintain the existing competition between the applicants in these markets for the most time-sensitive travellers. We propose to implement this objective by attaching our standard "carve-out" condition to our approval. This condition would limit our grant of immunity so that it does not extend to pricing, inventory, or yield management coordination, or pooling of revenues with respect to unrestricted coach-class fares or any business or first-class fares for local U.S. point-of-sale passengers in the nonstop Chicago/DFW-London Heathrow and DFW-London Gatwick overlap markets.

In the other two overlap markets, New York City/Boston-Heathrow, we expect other U.S. airlines will enter if they can obtain the necessary slots and facilities at Heathrow. Continental has a hub at Newark, which would support its service to Heathrow, and Delta operates a significant level of international service at JFK and has a major presence at Boston. We have therefore tentatively decided to earmark three of the slots allocated to Delta and three of the slots allocated to Continental for new competitive nonstop service between New York-Heathrow and Newark-Heathrow, respectively. To address the substantial loss of competition at Boston, we have tentatively decided to allocate an additional slot to Delta earmarked for new competitive nonstop service in the Boston-Heathrow market. We have also tentatively decided to require bmi to provide United with the slot needed to permit United to operate an additional daily nonstop roundtrip in the Boston-Heathrow market. The evidence in this proceeding indicates that implementation of the proposed United/bmi alliance would not substantially reduce competition in any relevant market, either standing alone or in conjunction with the implementation of AA/BA. However, the evidence also shows that the United/bmi alliance would benefit from the

²²⁵ DOJ Comments at 43-44.

approval of both. We believe that it is in the public interest for that alliance to pass the benefits on to consumers in the form of improved service and competition in the Boston-Heathrow market. We expect that Continental's hub at Newark and Delta's substantial level of operations at JFK and Boston will enable them to compete effectively with AA/BA in the New York City/Boston-Heathrow markets.

Accordingly, we have tentatively decided to allocate six slots to service at New York, three for Continental at Newark and three for Delta at Kennedy. We tentatively find that three daily flights by each of these carriers provide the necessary competitive presence by new Heathrow entrants in this market. Similarly, we tentatively find that the Boston-Heathrow market requires one additional daily service from a new entrant in the market; we accordingly propose to allocate one daily slot to Delta for use at Boston.

G. Public Interest and Public Benefits Analysis

As conditioned by us, we think that the AA/BA alliance should not result in a substantial reduction in competition in any market. We recognize, however, that the alliance will eliminate one competitor in the Los Angeles-London market and that carve-out conditions may not provide a complete solution for the loss in competition in the Chicago/DFW-London Heathrow and DFW-London Gatwick markets. We find, however, that the alliance, subject to additional slot divestitures, will provide public benefits not otherwise obtainable and that it will not be adverse to the public interest.

The primary public benefit obtainable from our conditional approval of the AA/BA alliance is the opportunity to enter into a new Open Skies agreement with the United Kingdom. The U.S.-U.K. is our largest transatlantic aviation market. The United Kingdom is our largest transatlantic trading partner. The Bermuda 2 agreement governing air service in the market has for many years imposed suffocating restrictions on U.S. carrier initiatives in the U.S.-U.K. market to the detriment of our consumers, communities, and economies. Consequently, one of our most important international aviation policy objectives has been, and continues to be, to replace Bermuda 2 with an Open-Skies agreement with no regulatory restraints on pricing and entry. Without an Open Skies agreement, the *status quo* will continue and Bermuda 2 will continue to impose severe restrictions on U.S.-U.K. air services.

We find that there are no other reasonable available means for obtaining an open skies agreement with the United Kingdom. The United Kingdom has indicated an unwillingness to negotiate an Open Skies agreement unless we approve and immunize the AA/BA alliance. In addition, the pending decision by the European Court of Justice raises the possibility that the opportunity to reach an Open Skies agreement with the British government may be limited, as we have explained earlier in this proceeding.²²⁶

While we are requiring a divestiture of slots on antitrust grounds, the divestiture of additional slots is essential to enable us to find that the alliance will not be contrary to the public interest. As discussed above, the restrictions imposed by Bermuda 2 bar all U.S. airlines except United and American from serving Heathrow. If we limited the conditions placed on our tentative approval to those needed to satisfy the statutory antitrust test, we would effectively ratify a situation where only those two carriers could meet the demands of the most valuable travellers

²²⁶ Order 2001-9-12 at 4.

for access to their preferred London airport. Such a result would be entirely unacceptable. As we stated before, approval of an AA/BA alliance must be coupled with *de facto* open skies at Heathrow. Only through the divestiture of additional slots to the U.S. airlines offering international passenger service can we achieve that result.

We will therefore tentatively require AA/BA to divest enough slots and facilities at Heathrow so that Northwest, Continental, Delta, and USAirways can operate flights to London's preferred airport from one or more of their hubs. This divestiture will achieve our precondition of *de facto* open skies. While our proposed divestiture requirement will not enable those airlines to offer the optimal number of flights, the record shows that once carriers begin serving Heathrow, they should have some opportunity to increase their slot holdings, and therefore to expand their operations, slowly and over time, notwithstanding the severe shortage of slots at Heathrow,

We tentatively believe that the record in this proceeding, both in terms of data and argument by parties, already amply supports the finding that there is an immediate need for allocation now in order to expedite the public benefits of new competitive entry.

We therefore tentatively conclude that nine daily round-trip slots, together with related ground facilities, should be allocated for use by four competing carriers that have expressed interest in the record as follows: two additional slots each to Delta and Continental, three to Northwest, and two to USAirways.²²⁷

We have already allocated slots to Delta and Continental to enable them to enter Heathrow from New York and Boston. The significant presence that Delta and Continental have at New York and Boston will enable them to offer network benefits with these slots. The additional two slots for Continental will enable it to supplement its three frequencies at its Newark hub with two more, to be used wherever the carrier thinks most appropriate, in Houston, Cleveland, or some other gateway. Similarly, Delta will have the same latitude to supplement its Kennedy operations with two more daily frequencies at a gateway of its choice — Atlanta, Cincinnati, or elsewhere. We agree with DOJ that allowing the carriers to decide where best to use these frequencies increases the market efficiency of the remedy.

We tentatively find that Northwest should be able to mount at least three daily frequencies, from whichever hub or hubs it chooses. We propose that US Airways should receive two such opportunities, the most it suggested it would be prepared to inaugurate at any one gateway; as with the others, however, it will be free to use the opportunities at whatever hub or hubs it wishes.

We tentatively agree with the Department of Justice that the Boston market also requires an additional competitive remedy. There are two sources of competition with the AA/BA alliance that might be used to mitigate the anti-competitive effects of that alliance: the Star alliance between United and bmi, which we are also considering here, and new Heathrow entry by other non-applicant carriers.

²²⁷ We believe that these proposed slot divestitures will adequately protect competition and ensure that we obtain *de facto* Open Skies at Heathrow. We recognize that the U.S. airlines opposing the alliance have urged us to require the divestiture of more slots. Northwest, for example, alleges that 448 weekly slots should be divested. Supplemental Reply of Northwest at 8. American, however, has been using only 224 weekly slots during the peak season. ACL/BAA Response, Attachment 5.

Our slot divestitures from AA/BA are not, however, alone sufficient to allow us to satisfy the public interest standard with respect to the Boston market. We therefore tentatively expect to rely on the UA /bmi alliance, as they indeed argue that we should, to provide crucial additional competition to the AA/BA alliance in the Boston market. We expect that this competition will create further public interest benefits, in the form of expanded services and competition, to allow approval of these transactions.

United now offers only a single daily round trip in competition with a total of five offered by American and BA. We therefore tentatively find that, not only should Delta's entry into the Boston-Heathrow market be facilitated, as DOJ has recommended, but also the United/bmi alliance should be strengthened as a competitor in that market. We therefore propose to require bmi to divest one Heathrow daily slot, and we initially allocate that slot to its alliance partner specifically for use in the Boston market. We would thus introduce the additional competition at Boston that DOJ has called for in part by building on United's existing Heathrow service.

Our proposed action would also create competitive options for consumers in those overlap markets where new entry is less likely. In this connection, one of the key features of our proposed action is that it would create the opportunity for new U.S. carrier nonstop Heathrow service at several new U.S. gateways used as hubs by Continental, Delta, Northwest, or US Airways. These new nonstop services create the opportunity for a large number of one-stop alternatives to the services provided by AA/BA in the overlap markets. Consequently, while our proposal does not provide for new nonstop competition in the Chicago and Dallas markets, which is preferred by time-sensitive travelers, it does provide for new connecting-service options that may partially offset the loss of competition that would otherwise occur in these overlap markets.

Our proposed action also promotes another important objective, creating the opportunity for consumers in virtually all regions of our country to benefit from a new open-skies agreement with the United Kingdom. It does that by providing for new network competition, and with it, the opportunity for U.S. carriers to provide passengers in markets other than the overlap markets with new travel options in the U.S.-Heathrow market. Continental, Delta, Northwest and USAirways have used their hubs to build strong domestic route systems. These hub-generated route systems should permit each of these airlines to improve the quality and level of service between interior U.S. points and Heathrow. This consideration coupled with the pricing freedom of an Open Skies agreement would significantly increase competition in the overall U.S.-Heathrow market.

Our proposed action will also promote two additional important U.S. international aviation policy objectives.

First, it will enhance the competitive position of U.S. cargo airlines and their service to shippers in international aviation markets. In this regard, we note that FedEx, one of the world's most successful private enterprises, supports the joint application "so long as the unfair regulatory restrictions [imposed by Bermuda 2] are removed." FedEx Answer, at 11.

FedEx states that it is "particularly concerned that none of the parties, including the Department of Justice, have fully addressed the immensely valuable benefits of open-skies to U.S. shippers and exporters. An open skies agreement will reduce costs and increase flexibility for U.S.

shippers by removing regulatory impediments to efficient air express/cargo routings . . . More efficient air express/cargo service between the United States and the United Kingdom would generate benefits and create jobs in all sectors of the U.S. economy.” FedEx Reply, at 2 and 3, (footnotes omitted).

Second, our proposed action will enhance the ability of the United States to negotiate an Open Skies agreement with the European Union should the EU Commission be granted a mandate to conduct those negotiations. With an Open Skies agreement with the U.K., the U.S. will have such agreements with all but three EU countries, thereby substantially enhancing our negotiating leverage.

Our proposed action should also provide consumers with additional benefits in other relevant markets. Our decision allows AA/BA to create a new alliance to compete with existing alliances, and therefore to provide consumers with additional service options in the U.S.-Europe market. Until recently, American relied on joint ventures with Sabena and Swissair to provide service between the United States and points in Europe, and to compete with other airlines and airline alliances in the U.S.-Europe market. AA/BA maintain that American has been forced to discontinue service to 47 points in Europe because Sabena and Swissair are no longer operating.²²⁸

We have addressed at length the civil aviation rationale for approving these transactions; we also believe that broader considerations of “international comity and foreign policy,” as our law explicitly recognizes, are relevant.²²⁹ In this case, the importance of the civil aviation markets involved directly reflects the importance of the bilateral relationship between the United States and the United Kingdom. The restrictive aviation regime now in effect between our two countries has for decades represented a glaring anomaly in the strong and long-standing economic, social, and political bonds that tie the United States and the United Kingdom. Our tentative decision here reflects the reality of the importance of facilitating the links of communication between our two countries by eliminating Bermuda 2’s restrictions on airline service between the United States and the United Kingdom. Opening up the transatlantic airline markets should strengthen our broader ties with the United Kingdom and therefore furthers the goal of international comity and supports our decision here.

H. Implementation

Having tentatively determined that divestitures of slots are necessary, we believe that there must be a means of implementing those divestitures before immunity can take effect. We tentatively find it necessary to exercise oversight of each of the four competing carriers’ efforts to obtain

²²⁸ We note, however, that the record would not support a finding that the AA/BA alliance would significantly benefit consumers by creating new connecting service possibilities for travellers between the United States and points in Europe, Asia, and Africa served beyond London. We have found in other cases that alliances between U.S. and foreign airlines usually provide substantial benefits for travellers using the European airline’s hub as a connecting point. For example, see Order 2001-12-18 at 16-17. Here, however, the lack of facilities at Heathrow and BA’s view of its most profitable opportunities mean that BA is reducing its connecting services at Heathrow and focusing on the more profitable nonstop markets. However, we find that, in light of the significant public benefits that will be derived from this transaction, the lack of these kinds of service benefits does not alter our decision in this case.

²²⁹ The Secretary shall disapprove an agreement that substantially reduces or eliminates competition, unless he finds that, *inter alia*, the agreement is necessary “to achieve important public benefits (including international comity and foreign policy considerations)” 49 U.S.C. § 41309(b)(1)(A) (2001) (emphasis added).

slots and facilities in time to begin service by November 1, 2002, the beginning of the winter season. First, if this part of our decision is made final, we would expect the AA/BA alliance partners to begin immediately to notify the gaining carriers of available slots to be divested upon the conclusion of this proceeding by no later than April 12, 2002. We expect that all parties to such process will proceed in good faith, bearing in mind the standards discussed below that are intended to define a useable slot. To oversee and encourage this process, we tentatively intend to require each recipient of slots and facilities to report to us periodically, at intervals to be determined, on the progress of its efforts to gain entry at Heathrow through receipt of divested slots. In this fashion, any unforeseen obstacles to the entry process can also be brought to our attention as soon as possible. Should efforts to gain entry appear to reflect less than good faith, we tentatively reserve the authority to reconsider the allocation of the slots and facilities in question. The applicants, of course, have every incentive to go forward, as immunity will not become effective until the competitors are able to enter the market. The gaining carriers have equal incentive so as to gain competitive entry quickly, since each is vying with the other.

Another step in the process will be the competitors' active participation in all allocation procedures for Heathrow slots, which begin with the IATA slot conference for the next winter season in June. We expect the new entrants to use opportunities to obtain more useable slots in this more traditional fashion, including authorized trading of slots gained through divestiture. We do not expect new entrants to provide compensation in those slot trades, nor does this remove, in any way, the requirements of this order for AA/BA to provide slots and facilities for 16 daily round-trip services at times useable for transatlantic services.

Timing is a critical issue in the circumstances of this proceeding. American and British Airways have established a strong presence in these markets. Together, they operated 34 daily nonstop roundtrip flights in the overlap markets last summer. Both airlines have developed the marketing resources needed to support their very high level of operations. The proposed alliance would provide AA/BA with the ability to use their strong presence and resources to exercise market power in the overlap markets if other airlines have not been able to enter the Heathrow markets.

We are not specifying the precise slot times that the AA/BA alliance must initially offer. Nor do we expect that each U.S. airline receiving slots will necessarily get optimal timings. We recognize that, at slot-controlled airports around the world, airlines accept and operate flights at slot times that are not precisely what they have requested. As discussed above, we expect the airlines receiving slots from the AA/BA alliance to use the existing slot allocation procedures to try to improve any less than optimal timings. Our goal is to reflect, to the maximum extent possible, what airlines interested in entering a market would accept.

However, we also recognize as Northwest points out in its November 2, 2001 answer (Answer at 24) that although airlines with substantial service in a market can operate some flights at nonstandard times (daylight flights in addition to the expected evening transatlantic departures), airlines with only a limited amount of service must offer flights at the preferred times. Therefore, to fulfill our requirement that the competition lost through approval of the AA/BA alliance be mitigated, and that there be *de facto* open skies, the slots that the new entrant U.S. carriers at Heathrow ultimately hold must be "useable." No generally accepted definition of what constitutes a useable slot exists, and to some extent, it depends on an airline's specific circumstances in a given market. However, some existing parameters can provide guidance.

When slots were required for international services at Chicago's O'Hare Airport, and domestic slots could be withdrawn to accommodate international services, the Federal Aviation Administration would not withdraw a domestic slot if a vacant slot was available within one hour on either side of the time requested for the international flight. At New York's Kennedy Airport, most international services were accommodated at or near their requested times during the five slot-controlled hours. However, since the FAA did not withdraw slots at Kennedy, it was possible that, if there were no vacant slots, an airline requesting a slot in the middle of the slot-controlled period would have to operate two and a half hours away from its preferred time. Under the European Union Code of Conduct on Slot Allocation, a new entrant airline that does not accept a slot within two hours on either side of its requested slot time loses its new entrant status. In addition, the review mechanism in the European Union Code is triggered by the inability of airlines "despite serious and consistent efforts" to secure slots within two hours before or after their requested times.

Thus, both the U.S. and European approaches include a window of commercial usability around an airline's optimal operating time. For the purposes of this case, this operating window can be assessed from several bases: the time requested for the new Heathrow flights; the time any current Gatwick services are operated, if there is a difference; or the time that AA and BA operate flights.

VII. Tentative Decision on United/bmi Alliance

We tentatively find that implementation of the proposed UA/bmi alliance would not eliminate or substantially reduce competition. While United operates a substantial amount of U.S.-London service and bmi holds a large number of slots at Heathrow, bmi is a regional airline and operates no flights between London and the United States. bmi operates flights from Manchester to Washington, D.C., and Chicago, but Bermuda 2 prohibits bmi from serving U.S. points from Heathrow. None of the other foreign airline parties to this proposed alliance operate any flights between the United States and London.

Because Bermuda 2 bars bmi from entering any U.S.-Heathrow markets, and because bmi currently serves no U.S.-London markets, bmi is not an actual or potential competitor in the markets of concern in this case. See DOJ Comments at 3. The alliance between United and bmi accordingly will not cause a substantial reduction of competition in any market.

We do not agree with Delta's argument that bmi should be considered a potential new entrant competitor in the U.S.-Heathrow routes. Delta points out that in 1999 bmi applied to DOT for N.Y.-Heathrow exemption authority, and in that application stated that it was confident of its ability to enter and become a viable competitor in that market. Delta Answer, December 17, 2001, at 5-7. UA/ bmi have responded to Delta's contention by asserting that bmi has no current plans to enter the N.Y.-Heathrow market without a grant of immunity for its alliance with United. They state that bmi applied for the exemption authority in question in anticipation of a U.S.-U.K. mini-deal, and that bmi's strategy for providing N.Y.-Heathrow service has changed since that exchange of route rights failed to materialize. UA/bmi Reply, December 21, 2001, at 11-12.

Delta, Continental and Northwest argue that the proposed UA/bmi alliance would be anticompetitive because that alliance and the proposed AA/BA alliance would collectively dominate the U.S.-Heathrow market. The two proposed alliances would control more than 75

percent of the commercially viable slots at Heathrow, and they would operate more than 80 percent of the U.S.-Heathrow frequencies. *See, e.g.*, Continental Answer December 17, 2001, at 11.

We have found, as shown, that conditions must be imposed on the AA/BA alliance to prevent it from eliminating or substantially reducing competition in any market. We have tentatively found that our proposed conditions should effectively prevent significant competitive harm. We believe that the conditions that we have tentatively decided to impose on the AA/BA transaction will effectively address concerns about the impact of the proposed alliances on entry and competition at Heathrow. In addition, as discussed above, our approval of the UA/bmi alliance is conditioned upon bmi's divestiture of slots to us for the operation of a Boston-Heathrow flight, initially by United.

VIII. Tentative Grant Of Antitrust Immunity

We have the discretion to grant antitrust immunity to agreements approved by us under Section 41309 if we find that immunity is required by the public interest. It is not our policy to confer antitrust immunity simply on the grounds that an agreement does not violate the antitrust laws. However, we are willing to grant immunity if the parties to such an agreement would not otherwise go forward, and if we find that the public interest requires the grant of antitrust immunity.

The record shows that both Joint Applicants will not proceed with the Alliance Agreements without antitrust immunity.²³⁰ The Joint Applicants claim that they cannot accomplish the public benefits that they seek to achieve through the formation of this alliance absent antitrust immunity.²³¹ They state that the proposed integration of services will surely expose them to antitrust risk, since they fully intend to establish a common financial objective, permitting them to compete more effectively with other strategic alliances. Additionally, they point out that full operational integration will necessarily mean that they will coordinate all of their business activities, including scheduling, route planning, pricing, marketing, sales, and inventory control.²³²

Since the antitrust laws let competitors engage in joint ventures that are pro-competitive, we think it unlikely that the integration of either set of the Joint Applicants' services would be found to violate the antitrust laws, subject to the conditions being imposed. Nevertheless, the record suggests that the Joint Applicants could be subject to extensive and burdensome antitrust litigation if we did not grant their requests. The record also persuades us that they will not proceed without it.

While tentatively concluding that we should approve and give immunity to the alliances,²³³ we tentatively find, as discussed, that certain conditions are necessary to allow us to find that our actions in these matters are in the public interest.

²³⁰ AA/BA Joint Application at 33; and United/bmi Joint Application at 46.

²³¹ *Id.*

²³² *Id.*

²³³ The immunity that we propose to grant here would apply solely to transactions between the Joint Applicants and their wholly-owned affiliates. The immunity would not extend to code-share operations or other coordinated activities involved in such transactions to the extent applying to airlines other than the Joint Applicants and their wholly-owned affiliates.

IX. Other Issues

ACAA, a trade association for low-fare airlines, states that it supports the Department's initiatives to open markets and to expand opportunities for all U.S. airlines, and that it does not oppose the formation of alliances. However, it again argues that before any decision is made on AA/BA, the Department must ensure that domestic competition will be strengthened.

ASTA asks that the Department confer immunity on travel agencies who will be affected by the proposed AA/BA arrangement. It states that one of the effects from granting immunity to an alliance partnership has been to allow the affected airlines to coordinate with each other on marketing strategies and tactics and to agree on the commissions that they will pay travel agencies and other third parties who book their services, among other things. ASTA maintains that the immunizing process creates market power relationships among the airline partners that enable them to dictate terms to agents and compel agents to adhere to the airlines' policies and practices. ASTA maintains that the relief it seeks for travel agents would permit them to respond collectively to joint actions of the immunized airlines that are directly detrimental to the interests of those agents.

We are unwilling to grant ASTA's request that travel agencies be granted immunity so that they can jointly respond to the AA/BA alliance partners' efforts to develop a joint marketing program when that injures travel agencies. We are granting antitrust immunity to these alliances because we have found that these alliances, subject to the conditions imposed by this order, meet our statutory standards. The alliance partners, like the partners in any joint venture, may well wish to develop joint marketing strategies to further their common venture. ASTA has not attempted to show that any of the alliances approved by us have led to joint decisions on matters such as travel agency commission rates that would violate the antitrust laws. In these circumstances, we see no basis for granting the relief sought by ASTA.

We are also not granting the requests of ACAA that we take action in this proceeding to promote competition in domestic airline markets. This proceeding concerns the applicants' request for approval and antitrust immunity for an alliance agreement that will enable them to coordinate their services in international markets. Neither LaGuardia nor Washington Reagan National is a gateway for intercontinental service.

We have been investigating the complaints of anti-competitive behavior submitted by ACAA members, and no action need be taken in this proceeding on that issue. Finally, we are aware of the low-fare airlines' requests for changes to our rules on airline computer reservations systems (CRSs). We are working to complete our pending CRS rulemaking and are considering ACAA's proposals in that rulemaking.

IATA Tariff Coordination Issue

Consistent with our earlier decisions, it is contrary to the public interest to permit immunized alliances to participate in certain price-related coordination that is now immunized within IATA tariff coordination. We therefore tentatively condition our approval and grant of antitrust immunity to the Alliance Agreements by requiring both sets of Joint Applicants to withdraw from participation in any IATA tariff conference activities that affect or discuss any proposed through fares, rates or charges applicable between the United States and the foreign applicants'

homelands, or between the United States and any other countries designating an airline that has been, or is subsequently, granted antitrust immunity by the Department for participation in similar immunized alliances.²³⁴

Under this condition, the Joint Applicants may not participate in IATA coordination activities affecting fares, rates and charges between the United States and the United Kingdom, and between the United States and the homelands of their similarly immunized alliance competitors. Through prices between the U.S. and other countries, as well as all local fares in intermediate and beyond markets, are not covered by the condition.²³⁵

We tentatively find that this condition is in the public interest for a number of reasons. The immunity that is requested in the proceeding includes broad coverage of price coordination activities among the Joint Applicants. With respect to internal Alliance needs, tariff coordination through the IATA conference mechanism is duplicative and unnecessary. At the same time, one of the reasons that we tentatively find supports immunity for the proposed activities is the potential for increased price competition between the partners and other airlines, particularly other international alliances. We have tentatively found that such potential competition will, on balance, outweigh any potential anticompetitive effects of price coordination within the Alliances themselves and encourage the passing on of economic efficiencies realized by the Alliances to consumers in the form of lower prices. We have previously found that permitting the Joint Applicants to continued tariff coordination within IATA undermines such competition.

O&D Survey Data Reporting Requirement²³⁶

We have access to market data where our carriers operate, including markets that they serve jointly with foreign airlines, for example, the Department's Origin-Destination Survey of Airline Passenger Traffic (O&D Survey). We have also collected special O&D Survey code-share reports from several large alliances and have directed all other U.S. airlines to file reports for their transatlantic code-share operations beginning with the second quarter of 1996.

²³⁴ The condition currently applies to prices between the United States and the Netherlands; between the United States and Germany (see Order 96-5-27 at 17); between the United States and Denmark, Norway, and Sweden (see Order 96-11-1 at 23); between the United States and Austria (see Order 2001-1-19 at 16); between the United States and Chile (see Order 99-9-9 at 21); between the United States and Italy (see Order 99-12-5 at 3); between the United States and Belgium and Switzerland (see Order 2000-5-13 at 3-4); between the United States and Malaysia (see Order 2000-10-12 at 14); between the United States and Iceland (see Order 2000-10-13 at 16); between the United States and Panama (see Order 2001-2-5 at 14); between the United States and New Zealand (see Order 2001-4-2 at 3) and between the United States and France (see Order 2002-1-6). Also by letter dated May 8, 1996, Northwest and KLM indicated their willingness to limit voluntarily their participation in IATA (see Dockets OST-96-1116 and OST-95-618).

²³⁵ Under this condition, the partners could not participate in IATA discussions of the total ("through") price (see 14 C.F.R. §221.4) between a U.S. point of origin or destination and an origin and destination in Austria, Belgium, Chile, Denmark, France, Germany, Iceland, Italy, Malaysia, the Netherlands, New Zealand, Norway, Panama, Sweden, and Switzerland, or a homeland of a subsequently immunized alliance, whether such prices are offered for direct, on-line or interline service. They could, however, discuss local segment prices, arbitraries or generic fare construction rules that have independent applicability outside such markets. IATA activities covered by our condition would include all those discussing prices proposed for agreement, including both meetings and exchanges of documents such as those preceding meetings and those used in mail votes.

²³⁶ We will provide confidentiality protection for this data, as we do for international O&D data submitted by U.S. airlines. Although we will use this data for internal analytical purposes, we will not disclose it to any other airlines.

However, we receive no market information for passengers traveling to or from the U.S. when their entire trip is on foreign airlines, except for T-100 data for nonstop and single-plane markets. Such passengers account for a substantial portion of all O&D traffic between the U.S. and foreign cities, and the absence of such information severely handicaps our ability to evaluate the economic and competitive consequences of the decisions we must make on international air service.

We must also ensure that our grant of antitrust immunity does not lead to anticompetitive consequences. Consistent with determinations in similar cases,²³⁷ we have therefore tentatively decided to direct British Airways and British Midland and to continue requiring Austrian Airlines, Lauda, Lufthansa, and SAS, and their wholly-owned affiliates, to report full-itinerary Origin-Destination Survey of Airline Passenger Traffic for all passenger itineraries that contain a United States point (similar to the O&D Survey data already reported by American Airlines and United Air Lines).²³⁸

To prevent this reporting requirement from having any anticompetitive consequences, we have tentatively decided to grant confidentiality to the foreign applicants' Origin-Destination reports and special reports on code-share passengers. Currently, we grant confidential treatment to international Origin-Destination data. We provide these data confidential treatment because of the potentially damaging competitive impact on U.S. airlines and the potential adverse effect upon the public interest that would result from unilateral disclosure of these data (data covering the operations of foreign airlines that are similar to the information collected in the Passenger O&D Survey are generally not available to the Department, to U.S. airlines, or to other U.S. interests).

Our regulation, 14 C.F.R. Part 241 section 19-7(d)(1), provides for disclosure of international Origin-Destination data to air carriers directly participating in and contributing to the O&D Survey. While we have tentatively found it appropriate to direct the foreign partners to provide certain limited Origin-Destination data to the O&D Survey, the foreign partners are not air carriers within the meaning of Part 241. The regulation (14 C.F.R. Part 241, Section 03) defines an air carrier as "any citizen of the United States who undertakes, whether directly or indirectly or by a lease or any other arrangement, to engage in air transportation." The foreign carriers accordingly will have no access to the data filed by U.S. air carriers. Moreover, we will be making the foreign carriers' submissions confidential while maintaining the current restriction on access to U.S. air carrier Origin-Destination data by foreign air carriers.

Computer Reservations Systems (CRS) Issues

Another competitive issue concerns ownership interests that the Joint Applicants have in competing CRSs. The Joint Applicants have ownership and marketing ties with competing CRS firms. Therefore, as with the American Airlines-Sabena-Swissair arrangement (see Order 2000-4-22 at 18), the proposed integration of marketing operations of the Joint Applicants presents a risk that CRS competition may be reduced. In view of these factors, we tentatively find that any

²³⁷ For example, see Order 2001-1-19 at 16.

²³⁸ Consistent with our determinations in similar cases (see Orders 96-7-21, 96-11-1, and 99-9-9) we intend to request other foreign airline partners of immunized international alliances to submit O&D Survey data and condition any further grants of antitrust immunity on provision of such data. We will treat the foreign airlines' O&D data as confidential, will not allow U.S. airlines any access to the data, and will not allow the foreign partners in this case or other foreign airlines any access to U.S. carrier O&D Survey data.

grant of antitrust immunity for the Alliance Agreements should exclude the Joint Applicants' CRS interests and operations. We note that AA/BA recognize that immunity will not extend to their management of any interest they may have in individual CRSs and that United/bmi state that they do not intend to coordinate the management of their respective interests in the CRS systems owned and operated by Galileo International Partnership.²³⁹

Operation under a Common Name/Consumer Issues

Since operation of the Alliance Agreements could raise important consumer issues and "holding out" questions, if the Joint Applicants choose to operate under a common name or use "common brands," they will have to seek separate approval from the Department prior to such operations. For example, it is Department policy to consider the use of a single air carrier designator code by two or more airlines to be unfair and deceptive and in violation of the Act unless they give reasonable and timely notice of passengers of the actual operator of the aircraft.²⁴⁰

Exemption and Code-Share Authority

We have tentatively decided to approve the exemption and code-sharing portions of the joint applications. Consistent with Department practice, we propose to grant the underlying necessary exemption authority for a period of two years and to make the statements of authorization effective indefinitely, subject to our standard conditions.

No party has opposed the United/bmi code-share application. United, however, has specifically opposed approval of the AA/BA code-share application concerning third-country markets where there are agreed limitations on U.S. carrier code-sharing opportunities and no such opportunities are available for other U.S. carriers, as well as approval in other third-country markets where there is a lack of reciprocity or where other issues have made it impossible for U.S. carriers to offer code-share service. In this regard, United specifically cites AA/BA's proposed services beyond the U.K. to Turkey, France, the Ivory Coast, Ghana, Egypt, and South Africa.

The regulatory provisions applicable to our decision here, 49 USC §40109 and §212.11 of the Department's regulations, all require a finding that the authority is in the public interest. Except as noted below, we have tentatively decided to grant both joint applicants' requests for blanket code-share and related exemption authority. We tentatively find that the services proposed would provide valuable benefits to the traveling and shipping public as they would expand the price and service options available to travelers and shippers, and would provide additional or improved airline services. We also tentatively find that the public would benefit from coordinated passenger and baggage services available under the code-share arrangements. Moreover, we tentatively find that all of the services proposed here would be consistent with the anticipated open skies agreement between the United States and the United Kingdom.

We tentatively deny AA/BA's request for approval of code-sharing services in the U.S.-Istanbul, Turkey and U.S.-Cairo, Egypt markets. Those markets are currently subject to restrictions on third-country code-share services, and no opportunities are currently available.²⁴¹

²³⁹ AA/BA Joint Application at 55 (Docket OST-2001-10387) and United/bmi Joint Application Exhibit JA-1, section 4.10 (Docket OST-2001-10575).

²⁴⁰ See 14 C.F.R. Part 257.

²⁴¹ Services in the US-Turkey market are subject to phase-in provisions under the 2000 U.S.-Turkey Open-skies Agreement. We have recently solicited applications to use the opportunities for services in the April 2002-2003

We tentatively propose to grant AA/BA's request with respect to U.S.-France services. On January 22, 2002, the United States and France signed an Open Skies aviation agreement that now removes, among other things, all limitations on U.S.-France third-country code-share services. We also propose to grant AA/BA's request with respect to operations in the U.S.-Ghana market. Under the 2000 *ad referendum* agreement between the United States and Ghana, there are no limitations on the number of U.S. airlines that may provide code-share services. The number of code-share frequencies that U.S. carriers may offer, however, is subject to transitional limitations. Through March 31, 2002, 22 frequencies are available for U.S.-carrier services. Of these, seven frequencies have been allocated. As there are sufficient frequencies available for the proposed AA/BA services, we tentatively find no basis to withhold authority from the carriers for services in this market.²⁴²

We propose to defer action on AA/BA's request to operate code-share services in the U.S.-South Africa market. Under the U.S.-South Africa aviation agreement, four U.S. carriers may operate third-country code-share services. Currently, Northwest/KLM, United/Lufthansa, and Delta/Air France are authorized to conduct these services. One authorization remains available. American and Continental have filed applications to use the remaining authorization.²⁴³ Therefore, we will defer action on AA/BA's request to serve this market in this proceeding, pending resolution of the issues raised in those applications.

Finally, we also propose to defer action on AA/BA's request to operate code-share services involving the Ivory Coast. We have withheld action on requests to serve the Ivory Coast as a result of security concerns and propose to do the same here.

MISCELLANEOUS

We will deny the Motion of Continental, Delta, and Northwest to compel American and BA to produce additional documents.²⁴⁴ The three carriers request various reports on the question of BA's plans for operations, particularly short-haul, beyond London. We tentatively believe that there are only relatively modest beyond-U.K. benefits of this transaction; and we are not relying on any such benefits as a basis for approval. The documents sought by Continental, Delta, and Northwest are therefore not relevant to our decision.

period, the last year of the transition period. (See Notice dated January 7, 2002, Docket OST-2002-11273.) Therefore, we will not consider here their request for code-share authority in this market. In the U.S.-Egypt market, only three U.S. carriers may be authorized to operate third-country code-share services. Northwest, United, and Delta are the three U.S. carriers authorized for this service. See Orders 97-9-16 and 2000-11-2.

²⁴² See, March 28, 2000 Notice, soliciting applications for U.S.-Ghana services, Docket OST-2000-7194, and July 13, 2000 Notice of Action Taken, allocating frequencies to U.S. carriers. In the latter Notice, the Department specifically deferred action on an application by American for allocation of frequencies, pending approval of an underlying code-share arrangement with British Airways. Should we finalize our decision here, we would concurrently grant American's request in that docket for allocation of five weekly frequencies for U.S.-Ghana services.

²⁴³ See Dockets OST-99-6587 (Continental) and OST-99-6595 (American).

²⁴⁴ Emergency Joint Motion for the Production of Documents, filed December 14, 2001. This pleading was followed on January 15, 2002, by a Joint Motion for Immediate Action, in which the three movants exhort us to grant their motion immediately.

ACCORDINGLY,

1. We direct all interested persons to show cause why we should not issue an order making final our tentative findings and conclusions, granting approval and antitrust immunity, as discussed in this order, to the Alliance Agreements between American Airlines, Inc. and British Airways Plc and their wholly-owned affiliates, and to the Alliance Agreements among United Air Lines, Inc., British Midland Airways Limited, Austrian Airlines, Österreichische Luftverkehrs AG, Lauda Air Luftfahrt AG, Deutsche Lufthansa, AG, and Scandinavian Airlines Systems, and their wholly-owned affiliates, insofar as they relate to foreign transportation. The approval granted here is subject to the proposed limits and conditions indicated in the Appendix; and the condition that the antitrust immunity will not cover any activities of the Joint Applicants as owners or marketers of computer reservation systems businesses. In addition, the antitrust immunity for American Airlines and British Airways, and for United Airlines and bmi, is tentatively contingent upon their divesting 16, and 1, Heathrow Airport slots and ground facilities useable for transatlantic services, respectively, for use by other U.S. carriers for services to London Heathrow as detailed in this order;
2. We tentatively direct interested persons to show cause why we should not direct American Airlines and British Airways, Plc, and United Air Lines, Inc., British Midland Airways Limited, Austrian Airlines, Österreichische Luftverkehrs AG, Lauda Air Luftfahrt AG, Deutsche Lufthansa, A.G., and Scandinavian Airlines System, and their wholly-owned affiliates, to resubmit for review their Alliance Agreements three years from the date of issuance of the final order in this case;
3. We tentatively direct interested persons to show cause why we should not direct American Airlines and British Airways, Plc, and United Air Lines, Inc., British Midland Airways Limited, Austrian Airlines, Österreichische Luftverkehrs AG, Lauda Air Luftfahrt AG, Deutsche Lufthansa, A.G., and Scandinavian Airlines System, and their wholly-owned affiliates, to submit any subsequent subsidiary agreements implementing their Alliance Agreements for prior approval;²⁴⁵
4. We tentatively direct interested persons to show cause why we should not further condition our grant of approval and immunity to require American Airlines and British Airways, Plc, and their wholly-owned affiliates, to withdraw from participation in any International Air Transport Association (IATA) tariff conference activities that discuss any proposed through fares, rates or charges applicable between the United States and the United Kingdom, and/or between the United States and any other countries whose designated carriers participate in similar agreements with U.S. airlines that have been or are subsequently granted antitrust immunity by the Department;
5. We tentatively direct interested persons to show cause why we should not further condition our grant of approval and immunity to require United Air Lines, Inc., British Midland Airways Limited, Austrian Airlines, Österreichische Luftverkehrs AG, Lauda Air Luftfahrt AG, Deutsche Lufthansa, A.G., and Scandinavian Airlines System, and their wholly-owned affiliates, to

²⁴⁵ Regarding this requirement, we do not expect the Joint Applicants to provide the Department with minor technical understandings that are necessary to implement fully their day-to-day operations but that have no additional substantive significance. We do, however, expect and direct them to provide the Department with all contractual instruments that may materially alter, modify, or amend the Alliance Agreements.

withdraw from participation in any International Air Transport Association (IATA) tariff conference activities that discuss any proposed through fares, rates or charges applicable between the United States and the United Kingdom, Austria, Germany, Sweden, Denmark, Norway, and/or between the United States and any other countries whose designated carriers participate in similar agreements with U.S. airlines that have been or are subsequently granted antitrust immunity by the Department;

6. We tentatively direct interested persons to show cause why we should not direct American Airlines and British Airways, Plc, and United Air Lines, Inc., British Midland Airways Limited, Austrian Airlines, Österreichische Luftverkehrs AG, Lauda Air Luftfahrt AG, Deutsche Lufthansa, A.G., and Scandinavian Airlines System, and their wholly-owned affiliates, to report full-itinerary Origin-Destination Survey of Airline Passenger Traffic for all passenger itineraries that include a United States point (similar to the O&D Survey data already reported by American Airlines, Inc. and United Air Lines, Inc.);

7. We tentatively direct interested persons to show cause why we should not direct American Airlines and British Airways, Plc, and United Air Lines, Inc., British Midland Airways Limited, Austrian Airlines, Österreichische Luftverkehrs AG, Lauda Air Luftfahrt AG, Deutsche Lufthansa, A.G., and Scandinavian Airlines System, and their wholly-owned affiliates, to obtain prior approval from the Department if they choose to operate or hold out service under a common name or use "common brands";

8. We tentatively delegate to the Director, Office of International Aviation, the authority to determine the applicability of the directive set forth in ordering paragraphs 4 and 5 above to specific prices, markets, and tariff coordination activities, consistent with the scope and purpose of the condition, as previously described;

9. We defer action on the motions filed by American Airlines, Inc., British Airways Plc, United Air Lines, Inc., British Midland Airways Limited, Scandinavian Airlines System, for confidential treatment of certain data and information in their applications;

10. To the extent described in the text of this order, we tentatively grant American Airlines, Inc., British Airways Plc, United Air Lines, Inc., and British Midland Airways Limited, exemptions to operate in foreign air transportation of persons, property, and mail upon implementation of a U.S.-U.K. open skies aviation agreement and tentatively grant statements of authorization to conduct blanket, reciprocal code-share operations, subject to our standard applicable conditions;

11. We tentatively direct interested persons to show cause why we should not require all recipients of slots divested pursuant to this proceeding to report to the Director, Office of International Aviation, at intervals and in detail to be determined, on their progress in achieving entry at Heathrow Airport;

12. We direct interested persons wishing to comment on our tentative findings and conclusions, or objecting to the issuance of this order to file an original and five copies in Docket OST-2001-11029, and to serve a statement of objections or comments together with any supporting evidence the commenter wishes the Department to notice on all persons on the service list of this

docket no later than 21 days from the service date of this order. Answers to objections shall be due no later than 10 days thereafter;²⁴⁶

13. If parties file timely and properly supported objections, we will afford full consideration to the matters raised by the objections before we take further action. If no objections are filed, we will deem all further procedural steps to have been waived and will proceed to enter a final order;²⁴⁷

14. We deny the December 14, 2001, Emergency Joint Motion of Delta, Continental and Northwest and the January 15, 2002, Joint Motion for Immediate Action by these same parties;

15. We grant all motions for leave to file otherwise unauthorized documents; and grant the motions for confidentiality filed by all applicable parties with respect to their responsive pleadings in this proceeding; and

16. We shall serve a copy of this order on the parties to this proceeding, the Ambassador of Great Britain and Northern Ireland in the United States; the Department of State; and the Federal Aviation Administration.

By:

READ C. VAN DE WATER
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*

²⁴⁶ 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. In the alternative, filers are encouraged to use the electronic submission capability through the Dockets DMS Internet site (<http://dms.dot.gov>) by following the instructions at the web site. For the convenience of the parties, service by facsimile or email is authorized. Persons should include their fax numbers and email addresses on their submissions and should indicate the method of service on their certificates of services.

²⁴⁷ Since provision is made for the filing of objections to this order, petitions for reconsideration will not be entertained.

**PROPOSED CONDITIONS
GOVERNING THE ANTITRUST IMMUNITY
FOR THE ALLIANCE AGREEMENTS BETWEEN
AMERICAN AIRLINES, INC., AND BRITISH AIRWAYS, PLC.**

Grant of Immunity

The Department grants immunity from the antitrust laws to American Airlines and British Airways, and their affiliates, for their Alliance Agreements, as defined by this order, between American and British Airways and for any agreement insofar as it applies between those parties incorporated in or pursuant to the Alliance Agreements.

Limitations on Immunity

The foregoing grant of antitrust immunity shall not extend to the following activities by the parties: pricing, inventory or yield management coordination, or pooling of revenues, with respect to unrestricted coach-class fares or any business or first-class fares for local U.S.-point-of-sale passengers flying nonstop between Chicago (ORD)/Dallas/Ft. Worth (DFW)–London Heathrow and DFW-London Gatwick (LGW); or the provision by one party to the other of more information concerning current or prospective fares or seat availability for such passengers than it makes available to airlines and travel agents generally.

Exceptions to Limitations on Immunity

Despite the foregoing limitations, antitrust immunity shall extend to the joint development, promotion or sale by the parties of the following discounted fare products with respect to local U.S.-point-of-sale passengers flying nonstop between Chicago (ORD)/Dallas/Ft. Worth (DFW)–London Heathrow and DFW-London Gatwick: corporate fare products; consolidator/wholesaler fare products; promotional fare products; group fare products; and fares and bids for government travel or other traffic that either party is prohibited by law from carrying on service offered under its own code. For immunity to apply, however: (1) in the case of corporate fare products and group fare products, local U.S. point-of-sale non-stop traffic between Chicago (ORD)/Dallas/Ft. Worth (DFW)–London Heathrow and DFW-London Gatwick shall constitute no more than 25 percent of a corporation's or group's anticipated travel (measured in flight segments) under its contract with American-British Airways; and (2) in the case of consolidator/wholesaler fare products and promotional fare products, the fare products must include similar types of fares for travel in at least 25 city-pair markets in addition to Chicago (ORD)/Dallas/Ft. Worth (DFW)–London Heathrow and DFW-London Gatwick.

Definitions for Purposes of this Order

"Corporate fare products" means the offer of non-published fares at discounts from the otherwise applicable tariff prices to corporations or other entities for authorized travel. These discounts

may be stated as percentage discounts from specified published fares, net prices, volume discounts, or other forms of discount.

"Consolidator/wholesaler fare products" means the offer of non-published fares at discounts from the otherwise applicable tariff prices to (1) consolidators for sale by such consolidators to members of the general public either directly, or through travel agents or other intermediaries, at prices to be decided by the consolidator, or (2) wholesalers for sale by such wholesalers as part of tour packages in which air travel is bundled with other travel products. These discounts, in either case, may be stated either as net prices due the parties on sales by such consolidator or wholesaler, or as percentage commissions due the consolidator or wholesaler on such sales.

"Promotional fare products" means published fares that offer directly to the general public for a limited time discounts from previously published fares having similar travel restrictions.

"Group fare products" means the offer of non-published fares at discounts from the otherwise applicable tariff prices for the members of an organization or group to travel from multiple origination points to a single destination to attend an identified special event. These discounts may be stated either as percentage discounts from specified published fares or net prices.

Clarification of Scope of Limitation on Immunity

Under no circumstances shall the limitations on antitrust immunity set forth above be construed to limit the parties' antitrust immunity for activities jointly undertaken pursuant to the Alliance Agreements other than as specifically set forth in this Order. Immunized activities include, without limitation: decisions by the parties regarding the total number frequencies and types of aircraft to operate on the Chicago (ORD)/Dallas/Ft. Worth (DFW)–London Heathrow and DFW–London Gatwick routes, and the configuration of such aircraft; coordination of pricing, inventory and yield management and pooling of revenues, with respect to non-local passengers traveling on nonstop flights on the Chicago (ORD)/Dallas/Ft. Worth (DFW)–London Heathrow and DFW–London Gatwick routes; and the provision by one party to the other of access to its internal reservations system to the extent necessary for use exclusively in checking in passengers or making sales to or reservations for the general public at ticketing or reservations facilities.

Review of Limitations on Immunity

Upon application of the parties, the Department will review the limitations on antitrust immunity set forth above to determine whether they should be discontinued or modified in light of: current competitive conditions in the Chicago (ORD)/Dallas/Ft. Worth (DFW)–London Heathrow and DFW–London Gatwick markets; the efficiencies to be achieved by the parties from further integration that would be made possible by discontinuation of the limitations on immunity, when balanced against any potential for harm to competition from such a discontinuation; regulatory conditions applicable to competing alliances; or other factors that the Department may deem appropriate.