THE DEPARTMENT OF TRANSPORTATION

Response To

THE TRANSPORTATION RESEARCH BOARD
NATIONAL RESEARCH COUNCIL

ENTRY AND COMPETITION IN THE U.S. AIRLINE INDUSTRY: ISSUES AND OPPORTUNITIES
(Special Report 255)

In December 1998, the Transportation Research Board (TRB) of the National Research Council, responding to a Congressional mandate, began an independent study of airline competition issues to update its 1991 report, *Winds of Change: Domestic Air Transport Since Deregulation* (Special Report 230). The TRB convened an 11-member committee of distinguished aviation, economic, management, legal, and public policy experts. On July 30, 1999, the committee issued its report, *Entry and Competition in the U.S. Airline Industry: Issues and Opportunities* (Special Report 255), which contained a number of recommendations for furthering and safeguarding airline competition in the United States. These recommendations, which are discussed in Chapters 3 through 5 of the report, fall into three broad categories: (1) exploiting opportunities for airline entry and competition, (2) effects of airline alliances and partnerships, and (3) competition and entry in smaller markets. Each recommendation and the Department of Transportation's response is set forth below.

The TRB also discussed the Department's proposed *Enforcement Policy Regarding Unfair Exclusionary Conduct in the Airline Industry,* published in April 1998. The TRB did not make an overall recommendation on the Department's adoption of enforcement guidelines but agreed that the proposal had flaws. The Department has received over 5,000 comments on the proposed policy statement. The Department is reviewing both the comments and the TRB report and will, as required, submit a separate report to Congress in connection with taking any final action on the policy statement.

EXPLOITING OPPORTUNITIES FOR

AIRLINE ENTRY AND COMPETITION
[Chapter 3]

The TRB discussed the need to improve access to airports and airways, indicating that capacity shortages can limit new competition, particularly entry and expansion by low-fare carriers. Operational constraints, such as take-off and landing slots and perimeter rules, are inefficient means for allocating limited capacity. The TRB advocated taking steps to replace these controls with more cost-based pricing mechanisms, and to expend more funds on the development and introduction of capacity-enhancing technologies. It also supported changes in the Federal laws that limit foreign ownership and control of U.S. airlines and oversight of developments in the ticket distribution system.

SYSTEM CAPACITY AND OPPORTUNITIES FOR COMPETITION

The TRB's Recommendation: *Apply Federal and other funds to expand airport and airway capacity, particularly by investing in capacity-enhancing technology. The goal should be to use pricing both to finance expansion and to allocate capacity more efficiently. Employ both technology and pricing to encourage additional flights to and from underused secondary airports in major metropolitan areas. [TRB Report, p.3-25]*

The Department's Response: We agree with the TRB that inefficient use of airport and airway capacity creates, among other problems, an obstacle to new entry and greater competition in aviation.

Precisely because we think this is such a serious problem, the Administration has pushed for fundamental, structural reform of the FAA's air traffic control (ATC) system. The goal is to make our ATC system as efficient as it is safe. Through the expanded capacity that greater efficiency would provide, we can reduce delays, enhance airline competition, better serve under-served communities, and accommodate the enormous growth projected for this vibrant industry.

Fundamental reform, including cost-based user fees, would allow the ATC system to operate more like a business. Most important, and in keeping with the TRB's recommendation, the current financing mechanism—an excise tax on airline passengers—should be replaced with a system in which the actual commercial users of ATC services pay for them based on the cost of those services. This change, together with an assurance that the resulting revenue would be used exclusively for air traffic control, would create a strong incentive for efficiency in both the operation and use of the ATC system.

If properly designed and implemented, airport pricing policies could play a role in reducing congestion at the Nation's busiest airports. Congestion-based fees could, as the TRB report notes, serve to allocate scarce airport capacity more efficiently than is the case today, where

airport capacity is rationed primarily through flight delay and other administrative procedures, such as the High Density Rule.

The practical problems involved in adopting congestion-based fees are significant. As the TRB noted, calculating the costs imposed by air carriers on an airport and other parties during different times of the day would be difficult. Indeed, a lengthy period of experimentation may be required before an airport authority is in a position to adopt congestion-based rates and charges. It may also be costly and difficult for airports to modify binding legal agreements with air carriers that establish standards and procedures for adjusting airport rates and charges. Any such congestion-based rates or charges would have to be consistent with Federal laws and other legal requirements.

The Department would welcome the opportunity to more fully explore the concept of congestion pricing.

SLOT CONTROL AND AIRPORT PERIMETER RULES

The TRB's Recommendation*: Introduce pricing methods in place of administrative restrictions to manage airline access to some of the country's major airports. The emphasis should be on early substitution of pricing for current slot controls and perimeter limits on long-haul flights, with the goal of allocating scarce airport and airway space more efficiently and fairly among competing airlines and taking into account other technical and operational factors. [TRB Report, p.3-26]*

The Department's Response: In its 1999 Federal Aviation Administration reauthorization proposal, the Administration asked Congress to eliminate slot restrictions over a five-year period (by September 30, 2004) at three slot-controlled airports: Chicago's O'Hare International and New York's LaGuardia and JFK International. The statutory scheme for Washington's Reagan National Airport would remain in place until Congress chooses to address it. Once the slot restrictions are eliminated, airport managers would be in a better position to use their facilities more efficiently. Congestion-based fees are one tool for more efficient allocation of scarce airport capacity. Airport managers at the slot-controlled airports would then be in a position to alleviate some of the congestion and delay that now occur during peak travel periods.

The TRB recommendation that perimeter rules on long-haul flights be ended involves three airports: Washington's Reagan National, New York's LaGuardia, and Dallas' Love Field. The rules at Reagan National and Love Field were established by Congress, and the Love Field rule was liberalized by Congress in 1997; the rule limiting flights at LaGuardia was adopted by the Port Authority of New York and New Jersey to alleviate severe congestion problems at that airport. Any modification to the perimeter rules should be addressed by Congress.

In this regard, the Department has taken steps to ensure that airlines can take advantage of Congress' decision to allow more air service at Love Field, notwithstanding efforts by some local groups to block the new services authorized by Congress at that airport.

SUPPLY OF GATES AND OTHER AIRPORT FACILITIES

The TRB's Recommendations: *Airport operators should take steps to ensure sufficient gate supply for competitors, including buying back gates from dominant incumbents, if necessary. The Department of Transportation, which can identify airports where gate availability is a recurrent problem, should monitor them closely; moreover, Federal aid should be contingent on the airport having well-defined plans to ensure sufficient gate supply. At the same time, the Department should review, thoroughly, its own rules affecting the ability of airports to obtain and spend funds for passenger facilities and other capital requirements. [TRB Report, p.3-19] The Department should ensure that Federal rules governing airport funding and spending do not conflict with—but help to achieve—the goal of increasing the availability of gates and needed infrastructure at major airports. [TRB Report, p.3-26]*

The Department's Response: We share the TRB's belief that providing prospective entrants with access to gates and other facilities on reasonable terms results in more competition, which in turn, results in lower average fares and better service for air travelers. Our just-released report, *Airport Business Practices and Their Impact on Airline Competition*, describes how airport actions affect airline competition and the role Passenger Facility Charges (PFCs) have played in increasing airport capacity and enhancing airline competition. The report also identifies actions the FAA should take to improve the effectiveness of its airport assistance programs with respect to competition, including assuring that underused gates leased by tenant airlines are made available to competitors.

An air carrier's financial viability often depends on serving key business and leisure markets, which requires securing reasonable access to airport gates and other facilities. Our report describes the critical role airport business practices play in shaping airline competition. Indeed, certain airport business practices may make it more difficult for an air carrier to serve an airport or for incumbent carriers to expand their services. Many of the airport business practices in place today were adopted decades ago in response to specific financial, economic, or political factors. These conditions may no longer apply and, indeed, may now impair competition among air carriers. Some airport managers and local public officials recognize this fact and are building new terminal facilities and adopting new business practices to improve competitive opportunities for all air carriers.

Our report concludes that airport managers have a legal obligation to accommodate reasonable requests made by air carriers that want to begin serving these communities. Airport managers have the authority to ensure that gates and other facilities are fully used; they also have the financial tools (*i.e.*, PFCs) to expand their terminals to accommodate reasonable requests from

air carriers that wish to serve their communities. In this regard, the Department will be more vigilant in ensuring that all airports meet their legal obligation to accommodate all qualified airlines.

Our report also identified a set of "best" industry practices. If these practices were more widely adopted at the Nation's busiest airports, it would improve the airline competitive environment. To foster airline competition in their communities, airport managers should: (1) promote new entry and become "advocates for competition;" (2) closely monitor the gate-use practices of tenant airlines; (3) be willing to invoke "use-it-or-lose-it" authority (or "use-it-or-share-it" authority) if incumbent carriers are not fully using their gates; (4) provide new entrants with clear guidelines and a timeline as to what they must do to gain access to an airport and when they will be able to begin operations, and have clear standards as to what incumbent air carriers must do to expand their operations; (5) monitor all sub-lease agreements to ensure fees charged are reasonable; (6) create an environment where "third-party" contractors can provide competitive ground-handling and support services; (7) take action to recover gates when they become available and to convert gates and other facilities to common-use status; (8) work to ensure that majority-in-interest agreements do not prevent or delay projects that would promote competition; and (9) use tools provided by the PFC program to finance terminal expansion projects that provide greater opportunities for all air carriers to compete.

To provide airports with an additional source of revenue to undertake important capital development projects and to help ensure that PFC funds are used in ways that will promote competition, the Administration, in its 1999 FAA reauthorization, proposed that the cap on PFCs be raised from $3 to $5. Our legislative proposal also recommended certain changes to the PFC program, including requiring any large hub airport that sought to impose the full $5 PFC and is dominated by a single air carrier to submit a "competition enhancement plan." If the Department determined that the competition plan failed to address needs for enhanced competition at the airport, the airport requesting the higher PFC would not be allowed the full increase but, instead, would be limited to a PFC of $4. Additionally, in developing its revised airport-airline fees policy, the Department will consider whether fee guidelines may incorporate options for accomplishing the objective of increasing airport gate availability.

FOREIGN OWNERSHIP OF DOMESTIC AIRLINES

The TRB's Recommendation*: Restrictions against foreign citizens owning and operating U.S.-based airlines should be lifted. [TRB Report, p.3-20]*

The Department's Response: The TRB has identified the economic arguments for changing our ownership and control standards; in particular, the TRB points out that such a change would encourage additional investment in the domestic airline industry, which would increase competition. There are, however, serious concerns with weakening these requirements. First, there are implications for the continued availability of U.S. air carrier aircraft for national defense purposes and second, U.S. jobs might be lost if greater foreign ownership is allowed.

AIRLINE TICKET DISTRIBUTION SYSTEM

The TRB's Recommendation*: Aggressive efforts by airlines to police travel agent sales deserve further scrutiny, and might warrant new rules requiring public disclosure of extra commissions and other targeted incentives that can prejudice agents. In general, however, changes in the distribution system should be viewed as opportunities to enhance the system's overall benefit to consumers, and should not be dissuaded unless the neutrality and completeness of the distribution system are fundamentally threatened. The Department should remain alert to the possibility of such erosion, however. [TRB Report, p.3-24]*

The Department's Response: The Department is aware that changes in the airline distribution system can affect airline competition and the ability of consumers to obtain complete and impartial airline information. Because of the importance of these issues, we are monitoring changes in airline distribution practices and conducting our own study of airline computer reservations systems (CRS) and related airline distribution issues in connection with our pending review of our CRS rules. The potential impact of airline distribution practices on airline competition and consumers has also been the subject of recent reports by this Department's Office of the Inspector General on override commissions and by the General Accounting Office on changes in airline ticketing practices.

In our CRS rulemaking, we will investigate whether additional rules are needed to prevent airlines that dominate markets from using that dominance to deter travel agencies from booking customers on competitors and from giving travel agency customers complete and impartial advice. We will consider the TRB's recommendations in that rulemaking and in other proceedings as appropriate. It is quite possible, for example, that we would consider an airline's use of its dominant position in a market as leverage against travel agencies in that area in connection with our investigation of complaints that the airline is illegitimately attempting to exclude competition.

EFFECTS OF AIRLINE ALLIANCES AND PARTNERSHIPS ON COMPETITION [Chapter 4]

The TRB stated its concerns that code-sharing and other collaborative arrangements among large U.S. air carriers will result in undesirable consolidation among current or potential rivals. It was also concerned that global alliances between U.S. and foreign air carriers, particularly those for which antitrust immunity has been granted, may in the long-run do more harm than good by reducing competition in primary international routes and by making it more difficult for unaffiliated carriers to compete domestically as well as internationally.

DOMESTIC AIRLINE PARTNERSHIPS

The TRB's Recommendation: *All collaborative plans among major U.S. airlines should be subject to traditional, economic-based merger analyses by the Department of Justice, and these plans—even if they do not involve exchanges of equity or transfers of assets—should be subject to advance notification requirements similar to those required under the Hart-Scott-Rodino process. [TRB Report, p.4-8]*

The Department's Response: The Department shares the TRB's concerns about the continuing consolidation in the domestic airline industry. The TRB's focus was on the alliances that have been formed by the six largest domestic network airlines and how they may affect domestic competition. The TRB also expressed concern about the effects of airline marketing and distribution practices on competition. Clearly, any such alliance will affect traffic flows in many markets and thereby affect competition in those markets and at hubs dominated by a partner in an alliance. These developments are inextricably linked with other facets of the industry: some smaller carriers are being acquired by the major airlines while others are aligning themselves with major network carriers in similar marketing and code-sharing arrangements. Furthermore, the competitive implications of these events are not limited to domestic markets because reducing the number of large U.S. airlines may effectively reduce the number of large multinational alliances that could be supported given that a U.S. airline partner is a necessary component for any viable global alliance.

Alliances between domestic carriers are fundamentally different in two respects from alliances between U.S. and foreign carriers for which we have granted antitrust immunity. First, the alliances between U.S. and foreign airlines that have been approved have involved very little overlap. Most overlaps have consisted of a small number of gateway-to-gateway markets where their networks are linked; the alliances are essentially end-to-end mergers. Second, alliances between U.S. and foreign carriers provide a way for carriers to overcome the limitations of bilateral agreements, ownership restrictions, and licensing and control regulations which preclude carriers from expanding their multi-country networks in an economically viable fashion as demanded by network economics. By contrast, no such legal restrictions prevent any U.S. carrier from directly entering any U.S. market; thus, domestic alliances are not a necessary means of gaining market access.

The TRB recognized that the airline industry structure is changing incrementally through the piecemeal implementation of marketing arrangements and alliances and expressed concern about the possibility that such relationships between U.S. carriers "will strengthen and migrate toward mergers—de facto, if not de jure. . . ." [TRB Report, p.E-4] Clearly an effective assessment of these developments requires an agency with the expertise in carrier operating, marketing, and distribution practices necessary to evaluate how these inter-related marketing arrangements will shape the competitiveness of the domestic and global industry structures. More importantly, this task requires a legal framework that permits the agency to look at the effects of such incremental changes on the broader industry configuration rather than being

legally restricted to analyzing any given transaction within the limits of a narrow legal mandate. It is for both of these fundamental reasons that the Department believes that the present system for the review of these alliance relationships is both appropriate and successful.

Legislation would be required to implement the TRB recommendation that collaborative plans among major domestic carriers be subject to advance notification requirements similar to those required by the Hart-Scott-Rodino process. The Department is not certain that such a process change is necessary.

The Departments of Transportation and Justice already cooperate closely in evaluating the competitive consequences of collaborative actions by domestic airlines. Each Department independently evaluates such actions, but shares the results of its evaluation. The Department of Justice applies its antitrust law test to prospective code-share alliances while the Department of Transportation performs its own analysis which additionally considers the broader transportation policy implications for the industry's structure. We believe that the informal working relationship that exists between the Departments of Justice and Transportation works well, allows a more flexible response to the developments in a dynamic industry, and fulfills the TRB's goal of ensuring that domestic alliances do not substantially reduce competition.

The Department of Transportation has the authority (under 49 U.S.C. 41712) to determine whether a domestic airline alliance (or any other joint venture between airlines) is an unfair method of competition that should be prohibited. This authority allows the Department to prohibit an airline practice if the practice violates the antitrust laws or if the practice violates antitrust principles. Consequently, the Department retains the authority to investigate all existing and proposed code-sharing and frequent-flyer programs and, upon a finding that they violate Section 41712, to require their termination or to impose conditions or limitations on such arrangements.

As the TRB noted in its report, last year Congress enacted a statute (49 U.S.C. 41716) which requires major airlines to file certain types of joint venture agreements with this Department 30 days before such agreements may take effect. That statute specifies four types of joint-venture agreements—codesharing, frequent-flyer programs, blocked-space agreements, and certain long-term wet leases—that may not take effect until at least 30 days after a complete copy of the agreement has been submitted to the Department. The statute further permits us to shorten the waiting period or to extend it for up to an additional 150 days for code-sharing agreements and an additional 60 days for the other types of agreements. The Department reviews agreements during the waiting period to determine whether they should be changed to prevent competitive problems or, if changes are not possible or are unacceptable to the parties, whether enforcement action should be taken because the agreements would constitute unfair methods of competition in violation of Section 41712.

In the case of the Northwest/Continental frequent-flyer and code-sharing agreements, this Department, after reviewing the agreements in consultation with the Department of Justice,

allowed the code-sharing agreement to take effect without an extension of the waiting period, and allowed the frequent-flyer agreement to take effect without an extension of the waiting period after the two airlines agreed to change certain provisions that raised competitive concerns with both Departments. The Department of Justice has filed a suit challenging Northwest's acquisition of the controlling block of Continental's voting stock and is continuing to review the two airlines' code-share agreement.

With the exception of the frequent flyer and code-sharing agreements concluded between Northwest and Continental, all of the agreements so far implemented between the partners to each of the three major domestic alliances were implemented before the new statute took effect, so this Department could not use that statute to stay those agreements pending review. The United/Delta and American/US Airways alliances so far have involved a significantly smaller degree of coordination than the Northwest/Continental alliance.

The Department of Transportation continuously monitors competitive developments in the airline industry and has been examining information routinely filed by the domestic airlines in an effort to identify any changes that may be attributable to airline alliance efforts. The fact that two of the three domestic alliances are largely hybrid marketing arrangements makes the task of analyzing their effects difficult because the data routinely reported to the Department are not readily conducive to evaluating marketing alliances and do not fully capture and reveal their effects. Given the uncertainties about the competitive consequences of combining frequent-flyer and other marketing programs and whether any of these alliances will develop further, we are moving to learn more while at the same time we remain cautious about taking specific steps to intervene. We are now in the process of determining what additional information we need from the airlines.

ANTITRUST IMMUNITY

The TRB's Recommendation: *A two-part process should be established for reviewing and approving applications for antitrust immunity by international airline alliances. The Department of Justice should perform the initial review and then forward to the Department of Transportation only those applications acceptable on competitive considerations. The Department of Transportation then should review these applications with respect to other issues of public interest and international policy. In addition, the Department of Justice should perform follow-up critiques of immunized alliances approaching renewal. [TRB Report, p.4-16]*

The Department's Response: The U.S. deregulation experience demonstrates that the airline industry, by its very nature, is a network industry and that network competition produces far better service at lower prices in the vast majority of markets. Major carriers have learned that hub-and-spoke network systems are an efficient way to serve most city-pair markets—particularly longer-distance, less-dense markets. Infrastructure constraints, high operating costs, bilateral constraints, and ownership and control limitations preclude individual airlines from

building global systems. This explains the growth in transnational alliances, as airlines around the world link their networks to capture the enormous efficiencies of larger networks and provide and market improved service to an ever-wider array of city-pairs. The Department's *International Aviation Policy Statement* recognizes that the trend toward expanding international airline networks is an inevitable response to the underlying network economics of the industry and seeks to enable U.S. airlines to become early and significant players in this globalization process. Our foremost international aviation goal, after safety, is opening up international markets to the forces of competition.

The TRB's comments related to alliances between U.S. and foreign airlines acknowledged the potential benefits of such alliances and did not question the competitive effects of our actions to date in approving alliances or granting antitrust immunity. Rather, very broadly, the TRB appeared to question our strategy of linking antitrust immunity to open skies agreements.

Antitrust immunity permits airlines to link their operations closely so that they can develop "virtual" global aviation. True integration is now denied airlines from different countries in most cases because of the bilateral system. In all circumstances, we have granted antitrust immunity on a case-by-case basis. We have granted immunity only after finding that a proposed alliance would be pro-competitive, pro-consumer, and consistent with our aviation objectives. In order to obtain these benefits, we determined, in each case, that antitrust immunity was needed to implement the alliance and to avoid potential litigation. In addition, not only are requests for antitrust immunity subject to rigorous analysis prior to action, after approval the alliances are monitored by the Department to evaluate their competitive effects and to further our understanding of structural developments in the global industry.

The TRB expressed concern that the Department's analyses that show alliances produce very positive consumer effects have caused us to adopt an *a priori* favorable position on international alliances. On the contrary, the Department's experience underscores both the importance and appropriateness of a case-by-case approach, the successful implementation of which requires in-depth understanding of industry developments and their consequence. Thus, an open skies agreement is a minimum prerequisite, without which we will not even undertake the competitive analysis necessary to decide whether antitrust immunity should, or should not, be granted.

The TRB also expressed concern that we do not consider the potential effect of international alliances on the competitive structure of the domestic airline industry. The TRB believed that the number of international alliances will determine the number of domestic carriers that will continue as viable competitors and that unaffiliated U.S. carriers may not survive, or at least may not be effective domestic competitors.

We are mindful of the potential effects of international alliances on domestic competition. We do not, however, share the view that carriers will either be part of extensive global alliances or cease to exist. We find it very difficult to visualize the demise of Southwest Airlines, for

example, just because it is not a part of an international alliance. (In fact, it does not even interline with other U.S. air carriers.) Clearly multinational alliances will play a major role in international markets. However, just as occurred following domestic deregulation, other systems of service will survive and new types will emerge. In the mid-1980s, at a time of major domestic consolidation, there was concern that as few as three large network airlines would dominate domestic markets. This has proven to be unfounded, and we believe that competition will take various forms in international markets as well. It is perhaps more likely that the number of domestic U.S. carrier competitors will determine the number of large global alliances that are possible, rather than the reverse scenario that concerned the TRB. As the largest single aviation market, the United States is not only large enough to sustain major carriers that operate only domestic service (*e.g.*, Southwest), it is also large enough so that a U.S. airline will be a necessary component of any global alliance. Thus, any global alliance will require a U.S. airline partner, but not all U.S. airlines will have to be part of a global alliance in order to succeed.

As global aviation continues to develop and restructure, some carriers will adapt better than others. This is not a basis, however, for taking actions to inhibit the development of pro-consumer and pro-worker multinational alliances. The development of geographically broad hub-and-spoke networks domestically has made it difficult for other carriers to compete in many markets. But the solution is not to prevent the development of such networks that clearly benefit consumers and open U.S. job opportunities in many markets, but to take actions that are designed to enhance airline competition where necessary.

The TRB's solution of requiring a two-part process, with the Department of Justice performing the initial competitive analysis and this Department then reviewing those applications passed on by the Department of Justice, would require legislation. Currently, we consult with the Department of Justice during our review of alliances, and Justice also does its own independent competitive analysis. Regarding the recommendation that the Department of Justice perform follow-up reviews of immunized alliances, this Department welcomes any constructive critique of any development in the industry that may affect competition, but we see no reason to require such critiques.

We fully concur with the TRB that we should continue to review alliances in light of their effects on airline competition and all aspects of the domestic and international airline industries. Given the complexity of these alliance arrangements, evaluation of their effects on airlines and consumers alike requires a substantial level of in-depth knowledge of the latest developments in airline commercial operations. The TRB acknowledged the benefit of the knowledge and expertise that resides with this Department. It is precisely for this reason that we believe that the current process will achieve the competitive objectives identified by the TRB.

CRS LISTINGS OF CODESHARES

The TRB's Recommendation: *TRB recommends that the Department of Transportation consider revising existing Computer Reservations System (CRS) rules to prohibit listings*

of the same itinerary under more than one carrier's code when one of the major code-share partners—or its commuter affiliate—serves the entire itinerary. [TRB Report, p.4-7]

The Department's Response: The Department recognizes that a flight's position in CRS displays affects how many bookings will be made by travel agents on the flight. The Department intends to review display issues, including the listing of code-share flights, in its pending CRS rulemaking and will propose revised rules on this subject if appropriate. The Department amended its rules on CRS displays in December 1997 to address some of the display issues raised by airlines that do not have code-share relationships.

COMPETITION AND ENTRY IN SMALLER MARKETS [Chapter 5]

The TRB noted that, while most of its report concentrated on the larger markets and related ways to enhance competitive opportunities for airlines, smaller markets also offer chances for new competition. The TRB offered two recommendations for encouraging operations in small to medium-sized communities and for encouraging new airline entry in general.

NEW AIRLINE APPLICATIONS

The TRB's Recommendation: *The Department of Transportation should be sure that its own policies and practices are not among the unintended impediments. For example, its economic fitness determinations for a new airline's certification require an array of information describing the carrier's business plan, its equipment, fares, and intended markets. The committee was not able to discern the need for this specific information, but recognized that the required public filings could help an incumbent. If some of these filing requirements are no longer necessary to ascertain fitness, they should be lifted or relaxed as vestiges of the regulated era. Competitively sensitive information should be treated as confidential. [TRB Report, p.5-2]*

The Department's Response: We agree with the TRB's comments that information detailing a new carrier's business plan in a publicly filed application may give incumbent carriers an unfair advantage, allowing the incumbents time to develop a competitive response to the new carrier even before that carrier has an opportunity to start its own operations.

The Department needs information on a applicant's business plan in order to evaluate whether the applicant has reasonably projected the costs of operating its proposed new service. This information is necessary for the financial viability portion of the fitness test for new carriers. The Department requires applicants to demonstrate, based on their own service proposal, that they have access to sufficient financial resources to cover their pre-operating expenses and all expenses that will be incurred during the first several months of operations so as to minimize the financial risk to consumers when the airline begins operations.

However, even though this information is required by the Department for its analysis, we agree with the TRB that such information does not have to be revealed to the public. The Department's rules already provide for confidential treatment of business-sensitive information when an applicant requests it, and we have already granted several such requests. We now intend, as a routine matter, to permit new carrier-applicants to file their proposed business plans, listing the markets they wish to serve, the frequency of service, and the proposed fares, on a confidential basis. We have revised the "information packet" that we provide to prospective new carriers on how to prepare and submit applications to include instructions on what information may be filed on a confidential basis.

This action should encourage the investment community's interest in new airline ventures by protecting innovative business plans and other competitively sensitive information contained in new certificate applications.

LIMITED, EXCLUSIVE ROUTE RIGHTS

The TRB's Recommendation: *That communities be permitted to offer airlines exclusive but time-limited, rights to provide nonstop service in city-pair markets that have none. Brief "patents" of this kind might allay concerns that hub carriers will challenge them aggressively to protect their own hubs. Local residents also might be assured that the service will be sustained, although this might warrant local subsidies or other financial inducements. [TRB Report, p.5-3]*

The Department's Response: The TRB's proposal would require legislation because Federal statutory provisions (the Airline Deregulation Act, the airport improvement program grant assurances, and the prohibition against grant of exclusive rights) do not permit either the Federal government or a state or local government to award a specific carrier a "patent" to serve city-pair markets. Offering "patents" to airlines to provide service in city-pair markets that have none is a creative and intriguing idea for how under-served regions might attract better service. Although we have not yet had time to examine the proposal in depth, we think it deserves further study by both the Department and the Congress.

We have already begun to address the concerns about competition in small- and medium-size cities. The Administration's 1999 FAA reauthorization proposal would establish a $25 million, five-year pilot program for awarding funds directly to rural communities, subject to a 25-percent local match, to help them attract new airline service.

Smaller carriers' efforts to establish viable services into major hubs are sometimes blocked by the dominant carrier's refusal to provide joint fares or even interline baggage agreements. Such non-cooperation means inferior service for outlying communities dependent on service via the dominated hubs. The FAA reauthorization proposal would also require joint fares and interline agreements between major carriers and smaller carriers at dominated hubs.

The Administration’s proposal would also exempt regional jets from the High Density Rule at slot-controlled airports in FY2000, and eliminate the rule altogether in five years (other than at Reagan National). In addition, the Department's report on airline access to airport gates contains suggestions on how airports can accommodate new entrant airlines, potentially creating more opportunities for airline service from large metropolitan areas to medium and small cities.

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