**BEFORE THE**
**DEPARTMENT OF TRANSPORTATION**
**WASHINGTON, D.C.**

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| U.S.-U.K. ALLIANCE CASE | ) | Docket OST-01-11029 |

**JOINT CONSOLIDATED REPLY OF UNITED AIR LINES, INC., BRITISH MIDLAND AIRWAYS LTD., AUSTRIAN AIRLINES, DEUTSCHE LUFTHANSA AG AND SCANDINAVIAN AIRLINES SYSTEM**

Communications with respect to this document should be sent to:


SHELLEY A. LONGMUIR
Senior Vice President-International,
Regulatory, and Governmental Affairs
JONATHAN MOSS
Managing Director-International
and Regulatory Affairs
UNITED AIR LINES, INC.
P.O. Box 66100, WHQIZ
Chicago, Illinois 60666

TIMOTHY BYE
Company Secretary and Group Legal Director
ANTHONY A. DAVIS
Director, Industry and Government Relations
BRITISH MIDLAND AIRWAYS LIMITED
Donington Hall, Castle Donington
Derby, England DE74 2SB

PAUL PAFLIK
Head, Airline Alliances
VERONICA OSBEN-ORELLANA
International Relations Intercontinental
AUSTRIAN AIRLINES,
ÖSTERREICHISCHE LUFTVERKEHRS AG
Fontanastrasse 1
A-1107 Vienna
Austria

BRUCE H. RABINOVITZ
SHEILA C. CHESTON
JEFFREY A. MANLEY
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037-1420
(202) 663-6670 (phone)
(202) 772-6670 (fax)
jmanley@wilmer.com

Counsel for
UNITED AIR LINES, INC.
and
AUSTRIAN AIRLINES,
ÖSTERREICHISCHE
LUFTVERKEHRS AG
and
DEUTSCHE LUFTHANSA AG
(Lufthansa German Airlines)


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NICOLAI VON RUCKTESCHELL
Senior Vice President and General Counsel
ULRICH SCHULTE-STRATHAUS
Senior Vice President
Head of International Relations and
Environmental Affairs
DEUTSCHE LUFTHANSA AG
Flughafen-Bereich West
D-60546 Frankfurt/Main
Germany

MATS LONNKVIST
Vice President & General Counsel
ANNA GILLSTROM
Director, Government and External Relations
SCANDINAVIAN AIRLINES SYSTEM
Frösundaviks Allé 1, Solna
S 195 87 Stockholm
Sweden

MARSHALL S. SINICK
ROBERT D. PAPKIN
SQUIRE, SANDERS & DEMPSEY L.L.P.
1201 Pennsylvania Avenue, N.W.
Suite 500
Washington, D.C. 20044
(202) 626-6651 (phone)
(202) 626-6780 (fax)
msinick@ssd.com

Counsel for
BRITISH MIDLAND AIRWAYS LIMITED

MICHAEL F. GOLDMAN
SILVERBERG, GOLDMAN & BIKOFF
LLP
1101 30th St., N.W., Suite 120
Washington, D.C. 20007
(202) 944-3305 (phone)
(202) 944-3306 (fax)
mgoldman@sgbdc.com

Counsel for
SCANDINAVIAN AIRLINES SYSTEM
(SAS)

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United Air Lines, Inc. ("United"), British Midland Airways Limited ("bmi"), Austrian Airlines/Österreichische Luftverkehrs AG and Lauda Air Luftfahrt AG ("Austrian"), Deutsche Lufthansa AG ("Lufthansa"), and Scandinavian Airlines System ("SAS") jointly submit the following consolidated reply to the answers filed by various carriers and government parties in the above-captioned proceeding on December 14 and 17, 2001:[1]

## *I. Introduction*

On September 5, 2001, United and bmi joined with Austrian, Lufthansa and SAS in seeking approval of and antitrust immunity for an expanded alliance agreement centered on transatlantic services. The expanded alliance focuses primarily, but not exclusively, on services via bmi's hub at London's Heathrow Airport (hereinafter

[1] Answers were received from the U.S. Department of Justice ("DOJ"), American Airlines and British Airways jointly ("American/BA"), Continental Airlines, Inc., Delta Air Lines, Inc., Northwest Airlines, Inc., US Airways, Inc., Virgin Atlantic Airways, Ltd., and cities of Dallas/Ft. Worth and Houston.

"Heathrow" or "LHR"). By adding bmi's Heathrow network to the existing immunized alliance among United, Lufthansa, SAS and Austrian, the carriers hope to offer an improved transatlantic alliance product for that subset of U.S.-Western Europe passengers that could be better served via London than via existing European alliance hubs in Germany, Austria and Scandinavia. bmi's Heathrow hub is well located to compete with other alliance hubs at Amsterdam and Paris. Moreover, the carriers recognized the need to improve their services at Heathrow in order to compete with the proposed American/BA alliance.

For bmi, the expanded alliance offers the opportunity for a relatively small regional carrier to enter London-U.S. markets. By using the existing services and U.S. sales network of United, bmi can link its own Heathrow hub with points in the U.S. at an acceptable level of commercial risk. Given the growing alliance relationship of BA, bmi's principal competitor at Heathrow, with American, bmi also foresaw the need for its own participation in an alliance network to be fully competitive as a transatlantic carrier.

United, bmi and their European partners have recognized that their expanded alliance would not be granted the antitrust immunity they require absent an open skies agreement between the U.S. and the U.K. Moreover, they also have recognized that no open skies agreement is achievable with the U.K. government without the ability of BA to obtain antitrust immunity for its own alliance with American. The Department in this consolidated proceeding is now primarily addressing the conditions that must necessarily be imposed on the American/BA alliance in order to ensure that an open skies agreement with the U.K. produces the competitive benefits for which it is intended.

The answers filed in this proceeding pursuant to the Department's consolidated procedural schedule are primarily focused on the competition issues raised by the American/BA alliance. United and bmi have consistently acknowledged that the American/BA alliance, because of the two carriers' relatively large Heathrow-U.S. market shares and the number of their overlapping routes raises difficult competition issues that would need to be resolved before antitrust immunity could be granted. There is a fairly widespread consensus among the parties, other than American/BA, that conditions must be imposed on the approval of that alliance in order to replace the competition that would be foreclosed by their alliance in overlapping Heathrow-U.S. markets. There is also a consensus that the expanded United/bmi alliance raises no comparable issues. Indeed, the parties that addressed the United/bmi alliance merely argue that, without appropriate conditions on the American/BA alliance, the expanded United/bmi alliance could adversely affect the competitive market structure on Heathrow-U.S. routes.[2]

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[2] 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. All of the latter carriers already participate in an immunized and integrated alliance with United, which bmi is now joining. In the DOJ's words:

> The other parties to the UA/bmi transaction (Lufthansa, Austrian, Lauda and SAS) are European carriers that do not operate any services between the U.S. and London, although they do provide some service from LHR to cities in their home countries. Thus, there is no significant competitive overlap among the parties to the United/bmi transaction in any U.S. markets.

cont'd.

No party argues, as indeed it cannot, that the United/bmi alliance would reduce competition in any city-pair market. There are simply no markets in which United and bmi compete. The DOJ, the only impartial party filing comments on the alliances, has concluded:

> We do not oppose including immunity for the UA/bmi transaction as part of an otherwise beneficial trade. Approval of the UA/bmi alliance presents no appreciable harm relative to the status quo because bmi is currently not an actual or potential competitor in U.S.-London markets -- it is prohibited by Bermuda II from operating to the U.S. from its LHR base.

DOJ Comments at 3. Certainly, the DOT must give greater weight to the disinterested position of DOJ than to the self-serving positions of the other parties that have commented on these alliances.

The problem before the Department is how to condition the American/BA alliance so as to preserve competition without jeopardizing the ability to conclude an open skies agreement with the U.K. DOJ's comments offer helpful guidelines for such conditions. It is clear that once the necessary conditions have been settled upon, there is no impediment to approval of the expanded United/bmi alliance and implementation of an open skies agreement.

Some parties have suggested that certain of the conditions imposed on the American/BA alliance should also be imposed on the expanded United/bmi alliance. These suggestions relate primarily to the ever-vexing issue of slot divestitures at

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DOJ Comment at 8. As no party opposes the carriers' request to integrate the United/bmi alliance with United's existing alliance with Lufthansa, Austrian, and SAS, the balance of this Consolidated Reply focuses solely on the United/bmi alliance.

Heathrow. Because United/bmi are not part of the competitive problem at Heathrow, however, there is absolutely no basis for the Department to impose any slot divestiture conditions on United/bmi. Indeed, since United/bmi are committed to becoming a significant competitor to an immunized American/BA alliance, it would be counterproductive to require United/bmi to contribute any of their limited slot holdings to the solution of the competitive problems caused by the American/BA alliance. United/bmi have what one party calculates as less than 17% of the commercially viable slots at Heathrow compared to the American/BA share of nearly 42%. Exhibit NW-38. United/bmi have made clear that they require additional slots in order to grow at Heathrow to compete more effectively with an immunized American/BA alliance.[3] To require United or bmi to divest slots from their much smaller holdings would be fundamentally unfair and completely inconsistent with any rational competition policy.

Finally, at least one party has suggested that antitrust immunity for American/BA be phased into effect so that it does not become fully effective until the carriers receiving divested slots are ready to begin service. DOJ Comments at 54. United and bmi take no position on that phasing proposal except to note that it should have no applicability to the effectiveness of immunity for the expanded United/bmi

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[3] It is important to note in this regard that DOJ's recommendation that four daily slots be divested for new entry on the BOS-LHR route, and 14 daily slots for the JFK-LHR route, represents more slots than United currently is able to allocate for use on these routes given its limited slot holdings at LHR. If the Department adopts DOJ's recommendation and allocates slots to a single carrier in each market, United will face new competition on these routes from a carrier able to offer a higher level of daily service. In these circumstances, fundamental fairness suggests that United or bmi should also be eligible to receive additional slots to maintain their alliance's ability to compete on these and other routes.

alliance. bmi is no less a new entrant to U.S.-Heathrow routes than the non-incumbents that are demanding LHR slots through divestitures. bmi and its partners need the same head start as any other new entrant to build an alliance at Heathrow that can compete with a combined American/BA. In these circumstances, United and bmi should be allowed to implement their expanded alliance as soon as that is possible under a U.S./U.K. open skies agreement and without regard to any phasing that may be required for full effectiveness of immunity for American/BA.

## *II.* Argument

### *a. The alliance of United and bmi does not cause any loss of competition in U.S.-Heathrow markets.*

In opposing immunity for the United/bmi alliance, Continental, Delta and Northwest rely almost exclusively on a claim that the grant of such immunity, coupled with the grant of immunity to American and BA, would be anti-competitive. Nowhere in these pleadings do the opponents attempt to demonstrate, however, that the grant of immunity to United and bmi will reduce actual or potential competition in any specific city-pair market, with one exception.[4] Rather, the pleadings focus principally on the combined slot holdings at LHR of BA, American, bmi, United, and the 14 other carriers that participate in the Star and oneworld alliances.

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[4] The one exception is Delta, which claims that bmi should be deemed an independent, potential entrant on the LHR-JFK route. As explained below, however, this claim does not withstand even nominal scrutiny. But, even if bmi were thought to be a potential entrant on the route, the grant of immunity to the United/bmi alliance would still be entirely pro-competitive and pro-consumer because of the network benefits the alliance will offer consumers. *See, infra* at pp. 11-13.

There are several fundamental problems with this type of analysis. First, it assumes that the Department would grant immunity to American and BA without first taking steps to redress the loss of competition that would result from approving what amounts to a *de facto* merger of the two largest incumbents in the U.S.-London market. United and bmi, no less than Continental, Delta and Northwest, oppose the grant of immunity to American and BA unless the Department imposes appropriate conditions to preserve competition on U.S.-Heathrow routes and to facilitate access to LHR by competitors. With open skies and appropriate conditions, however, United and American will no longer be the only two U.S. carriers serving LHR-U.S. routes. In such a revised market structure, static comparisons of carriers' historic LHR slot holdings become meaningless for purposes of prospective competition analysis.

More fundamentally, however, the claim by Continental, Delta and Northwest that the grant of immunity to the United/bmi alliance would be anti-competitive is predicated on a series of assertions about slot holdings at LHR that are analytically flawed. Continental claims, for example, that LHR slot holdings are heavily concentrated and that approximately 75% of LHR slots are controlled by American, BA, United, bmi and the other carriers that participate in the Star and oneworld alliances. Continental Answer at 10. Northwest makes a similar claim, arguing that 75.4% of "commercially viable slots" at LHR are controlled by carriers that participate in the Star and oneworld alliances. Northwest Answer at 18.

What these claims fail to acknowledge, however, is that the high degree of concentration alleged is due almost exclusively to the fact that BA (and its affiliates) alone hold nearly 40% of all slots at LHR. See the Letter dated 15 October

2001, from Airport Coordination Ltd. No amount of slot share gerrymandering by the opponents of immunity can change the fact that United and bmi collectively hold only 16% of the available slots at LHR. Nor can creative accounting change the fact that United, the only one of the Star Alliance joint applicants that operates direct service to the United States from LHR, holds less than three percent of all LHR slots, and bmi less than 14%; by comparison, BA with nearly 3500 total weekly slots, holds nearly 300% more LHR slots than bmi.[5]

When United's and bmi's LHR slot holdings are disaggregated from those of BA, it is clear that the alliance proposed between United and bmi poses no risk to competition on U.S.-LHR routes. Indeed, the DOJ, which has carefully analyzed both the United/bmi and the American/BA alliances, has recognized as much since it has found that the United/bmi alliance poses no appreciable competition risk. DOJ Comments at 3.

No more persuasive is the opponents' claim that United and bmi should be denied immunity because United/bmi and American/BA collectively would dominate U.S.-LHR service.[6] Again, as with the opponents' LHR slot calculus, the logic

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

[6] The claim of increased concentration on individual American/BA overlap city-pair routes from the grant of immunity to United and bmi is even more misplaced. Based on CRS booking data, for the 12 months ended July 31, 2001, United's share of Boston-London local bookings, for example, was just 11%, compared with a combined booking

of this claim is inherently flawed, reflecting nothing more than the historic limitations of Bermuda 2, and BA's domination of LHR-U.S. service that is the core objective of that thoroughly discredited agreement.

For example, Continental's claim that American/BA and United/bmi operate 84% of LHR-U.S. frequencies (Continental Answer at 11), and Delta's claim that the two alliances would control 86% of all LHR-U.S. service, including 83% of Boston-Heathrow service, and 86% of New York-Heathrow service (Delta Answer at 10-11), reflect nothing more than the fact that BA alone operates nearly 40% of all U.S.-LHR service. See DL-UK-1. United, by comparison, operates just 24% of LHR-U.S. service, slightly less service than American. *Id.* bmi, of course, operates none. As a result, while the extension of immunity to American and BA would give the combined carrier a 63% share of the service operated historically between LHR and the U.S., the extension of immunity to United and bmi will increase United's historic share not at all.[7]

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share for American (19.6%) and BA (39.4%) of 59%. United's share of New York-London bookings was 11.5%, compared with a combined share for American (15.3%) and BA (29.1%) of 44.4%. As for Chicago, United's principal domestic hub, its booking share was just 21.2%, a lower share than either American (25.5%) or BA (27.7%), whose combined share was 48.2%. United/bmi Joint Application Exhibit JA-15. Thus, while a grant of immunity to American and BA poses a serious risk to competition, given that United had lower booking shares than either American or BA on three of the four LHR-U.S. American/BA overlap routes where United also operates -- Boston, New York, and Chicago -- it hardly follows that the grant of immunity to United and bmi would pose a similar threat to competition. On the fourth American/BA overlap route -- Los Angeles-LHR -- United had a lower booking share than BA, but a higher share than American.

[7] By aggregating American/BA and United/bmi statistics, Delta, Continental and Northwest seek to create the impression that these two alliances are seeking immunity with one another. That is, of course, not the case.

Stated differently, if American and BA were granted immunity and United and bmi were not, the four carriers' combined LHR-U.S. service share, based on historic operations, will be the same 86% that the opponents attribute to the grant of immunity to both alliances. Thus, while United agrees that the increase in historic concentration levels that results from the grant of immunity to American and BA poses a serious competition risk, the same simply cannot be said about the grant of immunity to United and bmi. On the contrary, the grant of immunity to United and bmi leads to no increase at all in historic concentration levels, which is, of course, the reason that DOJ is not concerned about the grant of immunity to United/bmi.

As a corollary, it is equally clear that any slot divestitures required to ameliorate this increase in concentration must come solely from American and BA, the alliance that causes the increase in concentration, and not from United or bmi, whose alliance causes no such increase. Certainly, there can be no justification in logic or equity for taking slots from United or bmi solely because the alliance between American and BA leads to a *pro forma* increase in concentration on existing U.S.-LHR routes where United currently competes with American and/or BA. Indeed, if LHR slots were taken from United or bmi under these circumstances, the same logic would justify the taking of slots at LHR from Virgin Atlantic because, with the grant of immunity to American and BA, those carriers plus Virgin Atlantic will "dominate" LHR, operating over 76% of all LHR-U.S. service, including 83% of LHR-Boston and LHR-Los Angeles service and 86% of LHR-JFK service. *See* DL-UK-1-3 and 5. Just as this supposed increase in concentration could not justify taking slots from Virgin Atlantic, it cannot possibly justify taking slots from United or bmi, which are no more responsible for the

supposed increase in concentration than is Virgin Atlantic. United and bmi, no less than Virgin Atlantic, pose no threat to competition on U.S.-London routes, as the DOJ clearly concludes in its Comments.

On the contrary, even with other U.S. carriers gaining access to LHR as a condition to the grant of immunity to American and BA, the alliance between United and bmi still represents the best means available to ensure effective network-to-network competition on U.S.-LHR routes. Only with a grant of immunity, however, will United and bmi (and their European alliance partners) be positioned to develop the integrated network of services at LHR that will provide a meaningful competitive counter-weight to the integrated network of transatlantic services American and BA will be able to offer.[8]

*b. bmi is not a potential entrant on LHR-U.S. routes.*

Despite Delta's claim to the contrary, bmi is not a potential entrant on LHR-U.S. routes without a grant of immunity for the expanded alliance with United. In its answer, the only specific route Delta identifies where it claims that bmi is a potential entrant is LHR-JFK. Delta bases this claim solely on the fact that bmi applied to serve the LHR-JFK route in 1999 in anticipation of a mini-deal between the U.S. and

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[8] Even though, with open skies and immunity, United and bmi will be uniquely positioned to offer a competitive alternative to American and BA, the full realization of that opportunity is still dependent on the carriers' ability to gain additional slots and facilities at LHR. *See*, United Consolidated Reply in Docket OST-01-10387, dated November 9, 2001, at 7-8. Thus, in order for bmi to fulfill the DOJ's forecast that bmi may be willing to offer competition between Miami and LHR to replace that lost through the grant of immunity to American/BA, bmi would still need to be allocated additional slots in order to do so.

the U.K. that would have allowed a limited amount of new entry on LHR routes. Even though bmi sought in its 1999 application to portray itself as a credible competitor on that route, no amount of understandable route proceeding hyperbole on its part can change the basic fact that bmi is a relatively small U.K. and intra-European regional carrier, with a limited fleet of wide-bodied, inter-continental range aircraft, no current long-haul, inter-continental operations or facilities at LHR, and no meaningful commercial presence in the United States.

It is worth noting, moreover, that when bmi sought this authority in 1999, it was not facing the prospect of having to operate LHR-JFK service in an open skies environment. On the contrary, bmi's application was predicated on the belief that all of Bermuda 2's restrictions on competition would remain in place, save only the absolute cap on the number of carriers allowed to serve certain LHR-U.S. routes. Now, however, it is facing the prospect of starting service under circumstances where entry on the route would be opened to other carriers, including Delta, and where American and BA, the two largest LHR-JFK incumbents, would be allowed to combine their operations under a grant of antitrust immunity.

In any event, DOJ concluded, based on its impartial review of available evidence, that under present competitive and regulatory circumstances, bmi was not a potential entrant on the New York-Heathrow route. And even if bmi were found to be a credible, independent potential entrant on this route under an open skies agreement, there would still be no basis for a finding that its alliance with United would substantially reduce competition between Heathrow and New York.

The DOJ has recommended, moreover, that if the American/BA alliance is granted immunity, those carriers be required to divest 98 weekly LHR slots to permit other U.S. carriers to operate 7 daily roundtrips between LHR and New York, to replace the competition lost by the extension of immunity to American and BA. This represents more daily Heathrow-New York service than United currently operates on the route. Assuming the Department adopts DOJ's recommendation, there would be no basis for a finding that the grant of immunity to United and bmi could substantially reduce New York-Heathrow competition, even assuming the Department found, contrary to all credible evidence and the conclusions of DOJ, that bmi was an independent potential entrant on the route.

c. *The claim that the grant of immunity will create a so-called Heathrow "duopoly" is misplaced.*

As noted above, several carriers object to what they term would be a "duopoly" for Heathrow-U.S. services if both United/bmi and American/BA were granted immunity. Quite apart from the fact that such claims are wholly unwarranted for the reasons discussed above, the Department need have no concern about a supposed "duopoly" so long as the American/BA alliance is properly conditioned as the DOJ has proposed. In fact, DOJ itself raised no concerns at all regarding a "duopoly at Heathrow or with the similar "collective dominance" argument raised by Virgin Atlantic. With other carriers free to compete on Heathrow-U.S. routes, which is the purpose of DOJ's conditions, there should be no competition concerns simply because two immunized alliances will be operating at Heathrow.

In fact, with two alliances, Heathrow would be more competitive than most hubs. Although BA dominates the airport with 38% of departures, bmi does operate a smaller hub at that airport. With only 12.5% of departures, however, bmi's hub is not fully competitive with BA's, particularly in the most popular long haul destinations to the U.S., which Bermuda 2 has prevented bmi from serving. bmi's decision to enter into an alliance with United is intended to make bmi's Heathrow hub more competitive with BA. By allying with United, bmi gains broad access to the U.S. through the seven U.S. gateways served by United from Heathrow, four of which are United hubs.[9]

The alliance of United and bmi will also make United's services at Heathrow more competitive with those of American and BA. This is all the more important in view of BA's alliance with American. BA already dominates Heathrow-U.S. services, operating nonstop to 11 points in the U.S. and offering 232 total daily departures from Heathrow to all destinations, compared to United's service to 7 U.S. points and 12 total daily departures to all destinations. The ability for United to integrate fully its U.S.-LHR services with bmi's LHR network of local U.K. and intra-European

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[9] Delta and Continental complain that bmi should have chosen a U.S. partner that was not a Heathrow incumbent. While such a choice might have benefited a Heathrow non-incumbent such as Delta, it would not have afforded bmi the broad access to the U.S. market which it sought. Delta, having lost the contest to be chosen as bmi's partner, now seeks to have the U.S. government interfere on its behalf by disapproving bmi's choice. It is not the proper role of the government, however, to intervene in such commercial decisions, but, rather to review their competitive impact. The DOJ has made such a review and has found that the bmi's choice of U.S. partner raises no competition issues. Delta, in effect, is urging DOT to reach a different decision in order to "strengthen" Delta's position at Heathrow. While Delta might arguably be strengthened, bmi would be correspondingly weakened by losing the benefits of United's superior Heathrow-U.S. services. Such a decision, while perhaps understandable from Delta's perspective, has no proper place in a governmental competition review.

services is necessary to enable United to remain a competitive factor after BA and American effectively merge their LHR and LGW operations.[10]

Although the other carriers complain of a supposed duopoly at Heathrow, they ignore the fact that, with two alliance hubs operating at Heathrow, both alliances will be better able to offer important competition to the opponents' European alliance hubs at Amsterdam and Paris. Heathrow's location offers more direct routings to the U.S. for passengers from points in the western regions of Europe such as the Benelux, France and the Iberian peninsula, as well as the British Isles. United's present European alliance hubs require more circuitous routings via Frankfurt, Vienna, or Copenhagen for passengers to the U.S. from these countries. By adding an alliance hub at Heathrow, United and its partners will offer a more attractive online product to passengers in these Western European countries and will be more competitive with the Wings alliance hub at Amsterdam[11] and the Skyteam alliance hub at Paris, as well as the oneworld alliance hub at Heathrow.[12]

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[10] Delta also argues (Answer at 9-12) that bmi's alliance with United will make it more difficult for new U.S. entrants to obtain slots at Heathrow by removing bmi as a potential source for such slots. Delta's argument assumes, contrary to reality, that bmi is prepared to cannibalize its relatively small Heathrow hub to benefit U.S. carriers. As DOJ has recognized, a carrier such as bmi is an unlikely source for Heathrow slots. Moreover, in order to expand its own services at LHR, either as part of an alliance or independently, bmi has said consistently that it would require additional slots.

[11] Continental, through its code-sharing alliance with Northwest and KLM, is now also in a position to take advantage of the Wings hub at Amsterdam.

[12] Delta argues (Exhibits DL-UK-11/12) that bmi will bring relatively few new points to United's European alliance not already served by its other partners. That argument ignores, however, the major benefit the addition of bmi's Heathrow hub offers cont'd.

The purported concern about an alliance "duopoly" at Heathrow is in the final analysis a red herring. So long as the alliance between BA and American is properly conditioned to address new U.S. carrier entry, the addition of another alliance hub at Heathrow will have a net positive impact on transatlantic, as well as U.S.-U.K., competition.[13]

*d. The United/bmi alliance will produce substantial network benefits for consumers.*

As DOJ points out in its answer, international airline alliances have the potential to benefit consumers by lowering prices and improving service. DOJ Comments at 45-46. These benefits are most likely in markets where the parties are primarily vertically related (that is, those markets where parties offer interline service). *Id.* In such markets, both academic studies and DOT's own analyses of international

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by improving transatlantic connections for passengers from Western Europe and making United's alliance more competitive with Delta's, Northwest's, and American's alliances.

[13] Continental (Answer at 13) goes a bit over the top by citing Michael Levine's testimony regarding issues such as "duopoly" as being more objective and reliable than those of other "experts" because he is the "only private expert on aviation competition submitting comments in this proceeding who is not being paid by a participant." While Mr. Levine may have contributed his comments on his own initiative and without additional compensation, he cannot be viewed as being any less disinterested than other experts with similar backgrounds such as Alfred Kahn and Daniel Kasper who have offered their own views on the proposed alliances. Mr. Levine has had a longstanding relationship with Northwest as an officer and consultant and his paid consultancy with that company continues through March 2003 unless he chooses to terminate it. *See, e.g.*, Northwest Airlines Corp., Definitive Proxy Statement, Schedule 14A, March 24, 1999, Employment Agreements at 18. While his views may be relevant, they are no more persuasive than those of other consultants on the theory offered by Continental that Mr. Levine is a wholly "disinterested" party.

alliances demonstrate that cooperation on the pricing of these interline services by alliance partners frequently results in significant fare savings for consumers.

In the present case, American and BA claim these benefits for their alliance, if granted immunity. DOJ finds, however, that the benefits claimed are significantly overstated, and likely to be overwhelmed, in any event, by the American/BA alliance's high potential for anti-competitive price increases on the large number of LHR-U.S. routes where American and BA are today horizontal competitors. *Id.* at 46-47. In this regard, DOJ identifies two important differences between the American/BA alliance and prior alliances that have been granted immunity: the competitive overlap markets here are significantly larger than the routes where connectivity benefits are likely, and American and BA have an incentive to reduce total capacity on the overlap routes, negating any benefit that might accrue from connecting the two networks together. *Id.* at 47-48.

Neither of these divergences from prior alliances is present in the case of the United/bmi alliance. Most notably, there are no competitive overlap routes between United and bmi. As a result, granting immunity to the United/bmi alliance, unlike the American/BA alliance, poses no risk to existing (or potential) competition. Furthermore, because as noted previously, the integration of United's and bmi's networks over LHR will enable the carriers to offer a more attractive online product in U.S.-Europe city pairs where United today is unable to offer such a product with its current alliance partners whose hubs are located in Central and Northern Europe, United and bmi have strong economic incentives to exploit those opportunities to the fullest extent possible. Thus, unlike American and BA, United and bmi have no incentive to reduce capacity on

routes connecting United's domestic hubs with LHR, as doing so would reduce the carriers' ability to accommodate increased flow traffic on these flights.

For that reason, any reduction of capacity by United/bmi on U.S.-LHR routes would be entirely self-defeating as it would undermine the carriers' ability to grow the size and scope of the network of services they can economically sustain via LHR, thereby reducing, rather than enhancing, United's and bmi's ability to compete with the American/BA alliance. Moreover, United already carries fewer local passengers on virtually all of the U.S.-LHR routes where it competes with American and BA. It would, therefore, be self-defeating for United to reduce frequency (or capacity) on those routes as doing so would only reduce further its ability to compete with an effectively merged American/BA for higher yielding passengers. Finally, unless bmi can extend its own network of services at LHR on to the United States, the parties will have failed to achieve one of the core objectives of their alliance. Such expansion by bmi will increase both the number of frequencies operated daily between LHR and the U.S. and the number of daily seats available, putting downward pressure on fares.

For all of these reasons, the United/bmi alliance is likely to produce the same substantial network benefits for consumers that DOT has found in prior alliance cases where it has granted the applicants antitrust immunity.

*e. The United/bmi alliance should be approved as soon as an open skies agreement has been concluded.*

United and bmi are aware that the U.S. and U.K. governments hope to conclude an open skies agreement as early as next month, assuming a resolution of the remaining issues, most of which relate to the conditions to be applied to the

American/BA alliance. In these circumstances, and given the consensus that the United/bmi alliance by itself raises no competition issues, the United/bmi alliance should be granted immunity as soon as the U.S./U.K. open skies agreement has been concluded.

DOJ suggests (Comments at 54) that the effectiveness of "any immunity order" should be deferred "until the carriers that receive the divested slots and facilities are in a position to begin new service to remedy competitive harm." While such deferral may be warranted in the case of immunity for American/BA, it is certainly not warranted in the case of immunity for the expanded United/bmi alliance. United/bmi and their alliance partners require no less of a head start in preparing for competition against a combined American/BA than do the new U.S. carrier entrants at Heathrow. bmi is itself a new entrant in U.S.-Heathrow markets and, in conjunction with its alliance partners, will make an important contribution to countering the loss of competition at Heathrow caused by the effective merger of American and BA. 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.

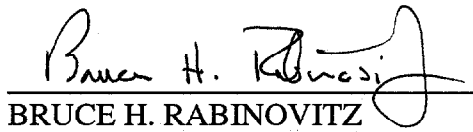
There is no reason, on the other hand, nor has DOJ or any other party offered one, for deferral of the immunity for the United/bmi expanded alliance. The rationale for DOJ's proposal to defer immunity for American/BA is based on the "immediate competitive harm" that would be caused by their combination. (DOJ Comments at 54). Because DOJ also concluded that the combination of United and bmi would result in no competitive harm, immediately or otherwise, there can be no claim

that there is any basis for a deferral of the United/bmi immunity as part of DOJ's phasing proposal.

### *III. Conclusion*

In conclusion, United and bmi, together with their European partners -- Austrian, Lufthansa and SAS -- urge the Department to approve and grant antitrust immunity for their expanded alliance agreement as soon as the U.S. and the U.K. have entered into the open skies agreement that is a prerequisite for such approval. Irrespective of whatever conditions and phasing may be deemed necessary for the effectiveness of any antitrust immunity granted the American/BA alliance, the grant of immunity for the United/bmi expanded alliance agreement and for coordination of that agreement with United's alliance with Austrian, Lufthansa and SAS should be effective immediately.

Respectfully submitted,



BRUCE H. RABINOVITZ
SHEILA C. CHESTON
JEFFREY A. MANLEY
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, DC 20037-1420
(202) 663-6670 (phone)
(202) 772-6670 (fax)

Counsel for
UNITED AIR LINES, INC.
and
AUSTRIAN AIRLINES,
ÖSTERREICHISCHE
LUFTVERKEHRS AG

and
DEUTSCHE LUFTHANSA AG
(Lufthansa German Airlines)

Michael F. Goldman/[illegible]

MICHAEL F. GOLDMAN
SILVERBERG, GOLDMAN & BIKOFF
LLP
1101 30th St., N.W., Suite 120
Washington, D.C. 20007
(202) 944-3305 (phone)
(202) 944-3306 (fax)

Counsel for
SCANDINAVIAN AIRLINES SYSTEM
(SAS)

Marshall S. Sinick/[illegible]

MARSHALL S. SINICK
ROBERT D. PAPKIN
SQUIRE, SANDERS & DEMPSEY L.L.P.
1201 Pennsylvania Avenue, N.W.
Suite 500
Washington, D.C. 20044
(202) 626-6651 (phone)
(202) 626-6780 (fax)

Counsel for
BRITISH MIDLAND AIRWAYS LIMITED

**DATED: December 21, 2001**

## CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the foregoing Joint Consolidated Reply of United Air Lines, Inc., British Midland Airways Ltd., Austrian Airlines, Deutsche Lufthansa AG and Scandinavian Airlines System on all persons named on the attached Service List by causing a copy to be sent via first-class mail, postage prepaid.

Brenda Gardner

Brenda Gardner

**DATED: December 21, 2001**

Megan Rae Rosia
Managing Director, Government Affairs
& Associate General Counsel
Northwest Airlines, Inc.
901 15th Street, N.W., Suite 310
Washington, D.C. 20005

USTranscom/TCJ5-AA
Attention: Air Mobility Analysis
508 Scott Drive
Scott AFB, IL 62225-5357

Carl B. Nelson, Jr.
Associate General Counsel
American Airlines, Inc.
1101 Seventeenth Street, N.W.
Suite 600
Washington, D.C. 20036

Roger W. Fones
Chief, Transportation, Energy &
Agriculture Section, Antitrust Division
U.S. Department of Justice
325 Seventh Street, N.W.
Suite 500
Washington, D.C. 20530

Simon Knight
First Secretary (Transport)
British Embassy
3100 Massachusetts Avenue, N.W.
Washington, D.C. 20008

Director of Flight Standards
Federal Aviation Administration
800 Independence Avenue, S.W.
Washington, D.C. 20591

Robert D. Papkin
Marshall S. Sinick
Squire, Sanders & Dempsey
1201 Pennsylvania Avenue, N.W.
Suite 500
Washington, D.C. 20004

John R. Byerly
Deputy Asst. Secretary for
Transportation Affairs
Department of State
2201 C Street, N.W.
Suite 5531
Washington, D.C. 20520

Robert E. Cohn
Alexander Van der Bellen
Shaw Pittman
2300 N Street, N.W.
Washington, D.C. 20037

Dennis E. Eckert
President and CEO
For the Cleveland Parties
Greater Cleveland Growth Association
Tower City Center
50 Public Square, Suite 200
Cleveland, OH 44113-2291

Michael Goldman
Silverberg Goldman & Bikoff, L.L.P.
1101 30th Street, N.W.
Suite 120
Washington, D.C. 20007

Nathaniel P. Breed, Jr.
For Federal Express
Shaw Pittman
2300 N Street, N.W.
Washington, D.C. 20037

Donald T. Bliss
For USAirways
O'Melveny & Myers
555 Thirteenth Street, N.W.
Washington, D.C. 20004-1109

R. Bruce Keiner
Crowell & Moring
1001 Pennsylvania Avenue, N.W.
Suite 1100
Washington, D.C. 20004

Edgar N. James
Marie Chopra
James & Hoffman, P.C.
1101 Seventeenth Street, N.W.
Suite 510
Washington, D.C. 20036

Daryl A. Libow
Sullivan & Cromwell
1701 Pennsylvania Avenue, N.W.
Suite 800
Washington, D.C. 20006

Don H. Hainbach
Boros & Garofalo, P.C.
1201 Connecticut Avenue, N.W.
Washington, D.C. 20036

Edward P. Faberman
Michelle M. Faust
Air Carrier Association of America
1500 K Street, N.W.
Suite 250
Washington, D.C. 20005-1714

Nicholas S. Penn
For the Houston Parties
Leftwich & Douglas, P.L.L.C.
1401 New York Avenue, N.W.
Washington, D.C. 20005-3922

David Stempler, President
Air Travelers' Association
5335 Wisconsin Avenue, N.W.
Suite 440
Washington, D.C. 20015-2034

Professor Darryl Jenkins, Director
The Aviation Institute
The George Washington University
School of Bus. & Public Management
600 21st Street, N.W.
Washington, D.C. 20052

J. E. Murdock III
Shaw Pittman
2300 N Street, N.W.
Washington, D.C. 20037

Rachel B. Trinder
Charles J. Simpson
Zuckert, Scoutt & Rasenberger
888 17th Street, N.W.
Washington, D.C. 20006

Chip Hallock, President
Regional Business Partnership
For the New Jersey Parties
744 Broad Street, 26th Floor
Newark, N.J. 07102

Elliott M. Seiden
Garfinkle & Wang PLC
1555 Wilson Blvd.
Suite 301
Arlington, VA 22209

Anita Mosner
Eclat Consulting
1555 Wilson Boulevard
Suite 602
Arlington, VA 22209

Paul M. Ruden
Senior Vice President
Legal & Industry Affairs
American Society of Travel Agents, Inc.
1101 King Street
Alexandria, VA 22314

Jon F. Ash
Managing Director
Global Aviation Associates, Ltd.
1800 K Street, N.W.
Suite 1104
Washington, D.C. 20006

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