

QA 24282

Order 97-6-30



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

Issued by the Department of Transportation  
on the 26th day of June, 1997

Served: June 26, 1997

**Joint Application of**

**UNITED AIR LINES, INC.**

**and**

**AIR CANADA**

**under 49 U.S.C. §§ 41308 and 41309 for approval  
of and antitrust immunity for an expanded  
alliance agreement**

Docket OST-96-1434 - 17

**ORDER TO SHOW CAUSE**

United Air Lines, Inc. and its regional commuter affiliates ("United"), and Air Canada and its regional affiliates have applied for approval and antitrust immunity under 49 U.S.C. §§ 41308 and 41309, for an Alliance Expansion Agreement ("the Alliance Agreement"),<sup>1</sup> whereby the Joint Applicants will plan and coordinate service over their respective route networks as if there had been an operational merger between the two airlines.

We have tentatively decided to grant approval of and antitrust immunity for the Alliance Agreement between United and Air Canada. We have, however, tentatively found it appropriate to condition our approval and to require supplemental information as more fully explained below. We propose to exclude from our approval and grant of antitrust immunity in this proceeding cooperative arrangements involving all-cargo services and cooperative arrangements involving service to third countries.<sup>2</sup> We propose to direct the

<sup>1</sup> The term "Alliance Expansion Agreement" includes the agreements between the Joint Applicants dated May 31, 1996 ("1996 agreement"), May 30, 1995 ("1995 agreement"), any implementing agreements which the applicants conclude pursuant to the 1996 agreement, and any other agreement or transaction by the applicants pursuant to the foregoing agreements. See Joint Application, footnote 1, and Exhibit JA-1.

<sup>2</sup> The predicate for our tentative approval and grant of antitrust immunity for the United-Air Canada alliance is the existence of a bilateral aviation agreement between the United States and Canada that provides for open transborder (*i.e.*, third- and fourth-freedom) markets, subject to a short-term phase-in period. Additionally, as more fully explained below, we have previously determined that the U.S.-Canada market is characterized by various distinguishing features that make it unique. Furthermore, to the extent that the U.S.-Canada market remains restricted beyond the phase-in period provided for in the U.S.-Canada agreement, we are unprepared to grant antitrust immunity. However, the Department would

37 pp

applicants to file all subsidiary and/or subsequent agreement(s) with the Department for review and to resubmit for review their various alliance agreement(s) in five years. We also tentatively find it in the public interest to direct Air Canada to report full-itinerary Origin-Destination Survey of Airline Passenger Traffic (O&D Survey) data for all passengers to and from the United States (similar to the O&D data already reported by United). By this order, we are providing the Joint Applicants and other interested parties the opportunity to comment on our tentative findings. We further propose to withhold antitrust immunity with respect to services relating to fares and capacity for particular categories of U.S. point-of-sale local passengers in the Chicago-Toronto and San Francisco-Toronto markets, as agreed between the Joint Applicants and the Department of Justice ("DOJ").

We tentatively find that, subject to the conditions and limitations specified, our action in this matter will advance important public benefits. Approval would permit the two airlines to operate more efficiently and to provide better service to the U.S. traveling and shipping public, and would allow United to compete more effectively with other carriers and alliances in U.S.-Canada transborder markets. With our proposed limitation of approval and immunity to these transborder markets, our proposed action will be consistent with our policy of facilitating competition among emerging multinational airline networks, where those networks will lead to lower costs and enhanced service for U.S. and international consumers. We fully recognize the trend toward expanding international airline networks, and our action here will further the goal of allowing our airlines to become significant players in the globalization of the airline industry.

Our proposed action in this order, as limited to U.S.-Canada transborder markets, is consistent with our approval and grant of antitrust immunity for the alliance between Northwest Airlines and KLM,<sup>3</sup> and with our recent grant of immunity for the alliance between American Airlines and Canadian Airlines International ("CAI").<sup>4</sup> Our experience with the Northwest/KLM alliance has demonstrated that such alliances between U.S. and foreign airlines can benefit consumers. The alliance between Northwest and KLM has enabled the two airlines to operate more efficiently and to provide integrated service in many more markets than either partner could serve individually.<sup>5</sup> Likewise, the alliances we approved in 1996 -- between Delta Air Lines, Austrian Airlines, Swissair, and Sabena<sup>6</sup> and between United, Lufthansa German Airlines, and Scandinavian Airlines System<sup>7</sup> -- are

---

consider lifting these restrictions on grant of immunity if and when the underlying market restrictions are removed.

<sup>3</sup> Orders 93-1-11 and 92-11-27.

<sup>4</sup> Orders 96-5-38 and 96-7-21.

<sup>5</sup> *International Aviation: Airline Alliances Produce Benefits, but Effect on Competition is Uncertain* (GAO/RCED-95-99, April 6, 1995); and *A Study of International Airline Code Sharing*, Gellman Research Associates, Inc., December 1994.

<sup>6</sup> Order 96-5-26 and Order 96-6-33.

<sup>7</sup> Order 96-5-12 and Order 96-5-27.

providing benefits to travelers and shippers. We expect that the alliance between United and Air Canada will also provide substantial benefits to consumers.

By this order we are also requiring the Joint Applicants to disclose information about the recently announced "Star Alliance" -- which is comprised of United Air Lines, Air Canada, Lufthansa German Airlines, Scandinavian Airlines System, Thai Airways International, and (in October 1997) Varig Brazilian Airlines -- and the possible impact of that alliance on this application for antitrust immunity. As discussed in section XI, *infra*, we will give interested parties an opportunity to comment both on our tentative decision and on the implications of the Star Alliance for the request for antitrust immunity.

## **I. Background**

### **A. The U.S.-Canada Aviation Agreement**

On February 24, 1995, the Governments of the United States and Canada signed a new Air Transport Agreement Between the Government of Canada and the Government of the United States. The new accord allowed any Canadian carrier to serve any point in the United States, effective immediately. It also allowed U.S. carriers to serve any point in Canada *except* (in the short term) Montreal, Toronto, and Vancouver. It also provided for open entry by U.S. carriers into those three Canadian cities, to be phased in over two years (at Montreal and Vancouver) or three years (at Toronto). The restrictions on U.S. carrier operations to Montreal and Vancouver expired February 24, 1997. At Toronto, during each of the first two years from the date of the agreement, the U.S. was able to select up to two additional carriers, with each carrier able to operate up to two daily round-trip frequencies. For the third year, the U.S. was able to select up to four more carriers, each with up to two daily round-trip frequencies, or alternatively increase frequencies of previously selected carriers. U.S. carriers will gain open-entry authority at Toronto effective February 24, 1998. The agreement also places frequency limits on code-sharing operations between the United States and Toronto. Similar limitations expired February 24, 1997, at Montreal and Vancouver, and the limitation on code sharing will expire February 24, 1998, at Toronto.

The purpose of the new U.S.-Canada agreement is to create an open transborder aviation environment between the U.S. and Canada. U.S.-carrier entry was temporarily restricted at the three largest Canadian gateways to give the national carriers of Canada an opportunity to adjust to the new competitive environment. As the earlier U.S.-Netherlands Agreement has demonstrated, open transborder operations should encourage more competitive service in U.S.-Canada transborder markets. Since the price and service quality of U.S.-Canada transborder airline service is becoming disciplined by market forces, not restrictive bilateral agreements, as the new agreement phases out entry restrictions, U.S.-Canada travelers will have multiple price and service options in choosing airline services available on transborder routes.

## **B. The Joint Applicants' Current Operational Relationship**

United and Air Canada began coordinated code-sharing service in September 1995. The Joint Applicants operate code-sharing service on several of their transborder routes and on certain behind- and beyond-gateway services. They also participate in each other's frequent flyer programs.

The applicants offer competing nonstop services with their own jet aircraft in the following five transborder markets:

- Chicago-Toronto
- Los Angeles-Vancouver
- San Francisco-Calgary
- San Francisco-Toronto
- San Francisco-Vancouver.

In the following 11 nonstop transborder markets one of the Joint Applicants operates flights which are sold under the codes of both United and Air Canada:

- Chicago-Montreal (jet service provided by Air Canada)
- Chicago-Ottawa (commuter service provided by Air Canada or its affiliates)
- Chicago-Vancouver (jet service provided by United)
- Chicago-Winnipeg (commuter service provided by Air Canada or its affiliates)
- Denver-Calgary (jet service provided by United)
- Denver-Vancouver (jet service provided by United)
- Los Angeles-Calgary (jet service provided by Air Canada)
- Los Angeles-Montreal (jet service provided by Air Canada)
- Los Angeles-Toronto (jet service provided by Air Canada)
- Washington-Ottawa (commuter service provided by Air Canada or its affiliates)
- Washington-Toronto (commuter service provided by Air Canada or its affiliates)

In addition, they offer code-sharing service in four of the five nonstop markets where they directly compete. United offers its code on Air Canada flights in the Chicago-Toronto and San Francisco-Calgary markets, and Air Canada offers its code on United flights in the Los Angeles-Vancouver, San Francisco-Calgary, and San Francisco-Vancouver markets. They also operate single-plane and connecting code-sharing service between seven interior (non-gateway) U.S. cities (United) and three interior (non-gateway) cities in Canada (Air Canada).

The Joint Applicants' current code-sharing agreement provides for the coordination of schedules, reservation systems, marketing and distribution, and frequent flyer programs over their code-sharing routes. Other forms of cooperation between the applicants, however, are limited. Each airline independently establishes its fares and rates for flights offered to the public under its airline designator code. As a consequence, the Joint Applicants engage in price competition over these code-sharing routes.

## II. The United-Air Canada Alliance Expansion Agreement

The Alliance Expansion Agreement established a contractual framework for significantly broadening and deepening the applicants' cooperation, permitting the two airlines to operate essentially as if they were a single firm. To that end, the agreement provides for the negotiation or creation of the following joint products:<sup>8</sup>

- (1) route and schedule coordination;
- (2) integration of marketing, advertising, and distribution services, including consolidation of global sales functions;
- (3) "co-branding" and joint product development;
- (4) pricing, inventory, and yield management coordination;
- (5) revenue sharing on certain routes;
- (6) joint purchasing and procurement;
- (7) coordination of ground and inflight services, including joint training of servicing personnel;
- (8) integration of belly cargo services, including express cargo products, joint facilities and terminals, revenue sharing, and coordination of ground handling and road feeder services;<sup>9</sup>
- (9) integration of information services, including inventory, yield management, reservations, ticketing, and distribution;
- (10) coordination and possible future integration of frequent flyer programs;
- (11) harmonization of financial reporting, including revenue and cost accounting practices;
- (12) development of common product standards, service levels, and inflight amenities; and
- (13) sharing of facilities and services at common airports.

The agreement also contemplates a division of responsibilities between the two carriers, with United operating joint services within the U.S. and Air Canada operating joint services within Canada. Both carriers will continue to provide transborder services. In short, the Alliance Agreement, if approved, will allow the two airlines effectively to operate much as a single firm, while retaining their individual identities regarding national ownership and control.

Finally, the Alliance Expansion Agreement requires that the applicants receive antitrust immunity for activities under the agreement before they may implement the agreement.<sup>10</sup>

---

<sup>8</sup> Joint Application at 9-13.

<sup>9</sup> Consistent with the Department's ruling in the American/CAI case, the Joint Applicants are not seeking antitrust immunity for joint all-cargo services. They do, however, seek immunity for belly cargo on combination passenger-cargo aircraft. Joint Application at 12, fn.28.

<sup>10</sup> Joint Application at 14.

### III. The Application and Responsive Pleadings

#### A. The Joint Application<sup>11</sup>

On June 4, 1996, United and Air Canada filed a request seeking approval of and antitrust immunity for the Alliance Expansion Agreement, for a five-year term.<sup>12</sup>

The Joint Applicants state that, through their Alliance Agreement, they intend to broaden and deepen their cooperation in order to improve the efficiency of their coordinated services, expand the benefits available to the traveling and shipping public, and enhance their ability to compete in the global marketplace. Although the Joint Applicants state that they will continue to be independent companies, they claim that the objective of the Alliance Agreement is to enable the airlines to plan and coordinate service over their respective route networks as if there had been an operational merger between the two companies. The applicants further assert that they will require approval and antitrust immunity for the agreement, inasmuch as proceeding with the agreement in the absence of immunity would present unacceptable risk of challenges under U.S. antitrust laws. Therefore, the airlines regard antitrust immunity as an essential condition precedent to implementation of the Alliance Expansion Agreement.

Through the Alliance Expansion Agreement, the Joint Applicants intend to develop an integrated global route network based on a multi-hub system, in order to achieve economies of scope and scale similar to those of domestic hub networks, and to pass those economies on to consumers in the form of lower fares and improved service.<sup>13</sup> To do so, the Joint Applicants must overcome regulatory and commercial constraints on development of international multi-hub systems. These include restrictions on foreign ownership and control and prohibitions of cabotage, which preclude the effective use of

---

<sup>11</sup> By Order 96-7-16, issued July 12, 1996, we found that the record of this case was substantially complete, and established further procedural deadlines. We also deferred action on the Joint Applicants' separate and joint motions for confidential treatment of certain data and documents (these motions were filed by United on June 19 and by Air Canada and the Joint Applicants on June 24, 1996), while limiting access to the information to counsel and outside experts who represent interested parties in this case.

<sup>12</sup> The Joint Applicants do not seek antitrust immunity relating to the management of their interests in their Galileo CRS system. In fact, their CRS systems are specifically excluded by the Alliance Agreement from coordinated services. They do, however, intend to harmonize their information systems, resources, and functions, including their internal reservations systems, inventory and yield management systems, and other distribution and operational systems. Accordingly, they do seek immunity to coordinate the presentation and sale of each other's services in CRS systems and to cooperate with regard to the operation of their internal reservations systems. The Joint Applicants claim that this is consistent with the Department's action in approving the Northwest/KLM alliance and the United/Lufthansa alliance. (See Orders 93-1-11 and 96-5-38.) Joint Application at 34-35.

<sup>13</sup> Joint Application, at 14.

mergers, joint ventures, or acquisitions, and the prohibitive investment in equipment, rights, and promotion, that would be required to build an international network *de novo*.<sup>14</sup>

The applicants assert that approval of and antitrust immunity for the Alliance Agreement are supported by substantial public and commercial benefits and efficiencies and by U.S. international aviation policy. In particular, the Joint Applicants cite our decision in the American/CAI case that approval would “be consistent with our policy of facilitating competition among emerging multinational airline networks, where those networks will lead to lower costs and enhanced service. . . ,”<sup>15</sup> and will encourage other countries to liberalize their bilateral aviation agreements with the United States.<sup>16</sup>

The Joint Applicants state that the alliance will create network synergies by (1) increasing the integration of their route networks; (2) enhancing the efficiency of their operations; and (3) facilitating seamless transportation service to the public. They argue that the alliance will produce expanded on-line connections, service improvements and lower prices through integration of yield management. It will also enable them to improve aircraft utilization, improve consistency of service, lower input costs through purchasing economies of scale, and reduce advertising, marketing, and other transaction costs.<sup>17</sup> The applicants maintain that they are prevented from attaining these benefits through merger because U.S. and Canadian laws concerning nationality and ownership effectively preclude mergers between U.S. and Canadian airlines. Accordingly, they can only achieve these efficiencies through a contractual alliance.<sup>18</sup>

The Joint Applicants also maintain that the grant of antitrust immunity will advance U.S. international aviation policy objectives by accelerating liberalization of the global marketplace, thus achieving an important goal of the Department’s “Open Skies” initiative. Further, the applicants assert that the Alliance Agreement is fully consistent with the Department’s policy of encouraging and facilitating the globalization and “cross-networking” of air transportation and with the newly liberalized Air Transport Agreement between the U.S. and Canada.<sup>19</sup>

They further contend that, because of the Department’s recent approval of and grant of immunity to the American/CAI alliance, “uniform, fair, and consistent application of regulatory policy” requires the Department to grant approval and immunity to the United/Air Canada alliance, to provide a level playing field in the U.S.-Canada market.<sup>20</sup> They further maintain that, if the Department were to fail to grant prompt approval of

---

<sup>14</sup> Joint Application at 14-15.

<sup>15</sup> Joint Application at 3 (citing Order 96-5-38 at 2).

<sup>16</sup> Joint Application at 17.

<sup>17</sup> Joint Application at 4-5.

<sup>18</sup> Joint Application at 5.

<sup>19</sup> Joint Application at 6.

<sup>20</sup> Joint Application at 7.

immunity, it would miss “the opportunity to take full advantage of the new aviation agreement with Canada to ensure the most competitive transborder market structure possible . . . ,”<sup>21</sup> and would create “a serious imbalance in the competitive structure of the transborder market,” and would give the American/CAI alliance an advantage over the proposed alliance.<sup>22</sup>

According to the Joint Applicants, the Alliance Expansion Agreement will lead to increased service, enhanced competition, and other consumer benefits, and will further the objectives of U.S. international aviation policy. They argue that the governing statute, 49 U.S.C. 41309(b), therefore, requires the Department to approve the agreement.<sup>23</sup> They further argue that grant of antitrust immunity is required by the public interest, because the Alliance Expansion Agreement will enable them to take advantage of the synergies produced by the linking of their networks, to provide seamless on-line services across their networks, to compete more effectively against the American/CAI and other alliances, and to provide the public with increased service options and lower prices.<sup>24</sup>

The Joint Applicants claim that the proposed alliance will not significantly reduce competition in any relevant market. In particular, they claim that their proposed alliance will increase competition in the overall U.S.-Canada market, already the most competitive bilateral aviation market in the world, by permitting them to offer on a joint basis new transborder services that neither carrier alone could provide.<sup>25</sup> Furthermore, unless United--which is only the fourth-largest U.S.-flag carrier in the transborder market--is permitted to combine with Air Canada, United will be unable to compete effectively with American for transborder traffic. Thus, unless the Department permits alliances to compete against each other, the Department’s recent approval of the American/CAI alliance would unfairly skew competition, and would be contrary to the public interest.<sup>26</sup>

Similarly, the Joint Applicants contend that the proposed alliance will not harm competition in any city-pair markets, as each of the five nonstop transborder markets where they now compete would continue to receive alternative nonstop service from other carriers. In addition, competing carriers would also continue to provide a large amount of one-stop and connecting services in these markets. Moreover, all transborder markets are or will soon be open to unlimited entry; this should further ensure the competitive nature of the five overlap markets.<sup>27</sup>

---

<sup>21</sup> Joint Application at 8.

<sup>22</sup> Joint Application at 2.

<sup>23</sup> Joint Application at 18.

<sup>24</sup> Joint Application at 19.

<sup>25</sup> Joint Application at 24.

<sup>26</sup> Joint Application at 25-26.

<sup>27</sup> Joint Application at 28-29.

In their application the Joint Applicants further contended that there is no basis for withholding grant of immunity in any of the markets where they now compete. Although the Department, in approving the American/CAI alliance, withheld immunity in the New York-Toronto market, the applicants argued that there is no basis for similar action here, as only one of the alliance partners (Air Canada) serves that market. Furthermore, in the Chicago-Toronto market, the Department granted immunity to the American/CAI alliance even though American was the largest carrier in the market. Accordingly, to compete effectively with the American/CAI alliance, the Joint Applicants claimed they must have similar immunity in the Chicago-Toronto market.<sup>28</sup> Finally, with respect to the other nonstop markets where the Joint Applicants compete, they claimed there is sufficient competing one-stop and connecting service to discipline the Joint Applicants' fares on these routes.

The Joint Applicants also assert that the proposed alliance will significantly increase on-line competition in behind- and beyond-gateway markets on both sides of the border. As a consequence, approval of the alliance -- like that of the American/CAI alliance -- will "benefit many passengers [that] now lack convenient on-line service. . . ."<sup>29</sup>

Finally, the Joint Applicants contend that they will not proceed with the alliance without antitrust immunity. They claim that the alliance will conduct joint marketing activities and price/service coordination throughout their systems. Notwithstanding the service enhancements and efficiencies these arrangements would create, the Joint Applicants categorically state that they could not carry out the full collaboration, coordination, and integration contemplated by the Alliance Expansion Agreement in the absence of antitrust immunity, inasmuch as there would be no assurance that the alliance would not subsequently be challenged on antitrust grounds. Since defending even a meritless antitrust suit would involve prohibitive costs and burdens on managerial time, the Joint Applicants will not implement the alliance without immunity.

## **B. Responsive Pleadings**

Answers to the joint application were filed on August 2, 1996, by American Airlines, Continental Airlines, Delta Air Lines, the International Air Transport Association, and Northwest Airlines. On August 13, 1996, the applicants filed a joint reply, and United filed an additional separate response.

### American

While not opposing the application, American does object to United's "blatant double standard," which American maintains would have the Department apply one set of rules to United and its allies, and another set of rules to its competitors. American notes that United "doggedly" opposed the American/CAI immunity application for a host of reasons.

---

<sup>28</sup> Joint Application at 30.

<sup>29</sup> Joint Application at 32-33, citing Order 96-5-38 at 20.

Yet, United now seeks antitrust immunity with Air Canada, which American states has almost six times as many transborder frequencies as CAI. Moreover, the combined United/Air Canada frequency share is more than double the share of American and CAI.

### Continental

Continental opposes the application. It maintains that approval would be “diametrically” opposed to the Department’s principles of (1) awarding U.S.-Toronto routes to strengthen U.S.-flag competition with Canadian airlines, (2) approving the American/CAI alliance to enhance competition with Air Canada, and (3) insisting on open-skies agreements before granting antitrust immunity to a dominant foreign carrier serving a market.<sup>30</sup> Continental notes that entry into the Toronto market continues to be restricted until February 24, 1998. Moreover, it states that the transborder alliances would lock up peak-period slots and facilities at Toronto before the transborder skies are open and develop formidable market presence that would make it extremely difficult for other U.S. airlines to compete effectively in the U.S.-Toronto markets. Under these circumstances, Continental maintains that the Department should deny approval of the United/Air Canada agreement, or at the very least, defer action on it until Canada agrees to far more open access between the United States and Canada.

### Delta

Delta opposes the application. Delta maintains that approval of an antitrust immunized alliance agreement between United and Air Canada (the dominant Canadian-flag carrier) in the absence of a full open-skies agreement with Canada that permits U.S. carriers both *de jure* and *de facto* open entry would represent a serious policy error. Moreover, the Department’s decision to approve an alliance agreement between American/CAI provides no predicate for approval of this application, since Air Canada, unlike CAI, dominates the overall Montreal/Toronto markets. Delta maintains that granting the application, absent full U.S.-Canada open skies, will give Air Canada and, by extension, United an unfair competitive advantage over other U.S. airlines by allowing them to benefit from the protective provisions of the bilateral agreement and a safe haven against competition by other U.S. carriers in the largest and most important Canadian markets.

Delta urges the Department to defer consideration of the application until February 24, 1998, the date full open-skies’ services may be provided in the U.S.-Canada marketplace. Delta notes that (1) the Department has established a firm policy to consider applications for immunity only where a fully effective open-skies agreement already exists; (2) former Secretary Peña had underscored the importance of open skies as a predicate to antitrust immunity; (3) open skies must be a pre-condition to consideration of applications for antitrust immunity in order to assure that the alliance would be subject to actual marketplace discipline; (4) the ability of U.S. airlines to organize competitive challenges to the United/ Air Canada alliance will not exist under the existing U.S.-Canada bilateral

---

<sup>30</sup> Continental notes that if the United/Air Canada application is approved, immunized alliances will control 99% of the traffic in the two largest U.S.-Canada markets (Chicago-Toronto and New York-Toronto) and nearly 60% of the total U.S.-Canada market (see Order 96-5-38, at 18-19).

agreement until February 28, 1998; and (5) the phase-in restrictions were expressly designed to give Air Canada a “head start” over U.S. airlines and to protect Air Canada from U.S.-flag competition in its primary markets.

Delta also asserts that, for the past two years, its service between Atlanta and Toronto has been limited to only two daily nonstop flights preventing Delta from matching Air Canada’s four daily nonstops. Furthermore, Delta notes that because of the restrictive character of the U.S.-Canada bilateral agreement, it is unable to serve the Toronto-Cincinnati market (Cincinnati is Delta’s second largest hub airport) in its own right (Delta provides services with commuter aircraft under a code-share arrangement on flights operated by Comair).

Delta states that approving the application would send other restrictive governments (such as the United Kingdom, Japan, and France) a message that those governments’ national airlines can obtain antitrust immunity for alliances even while those governments continue to insist on entry and other restrictions that protect those national airlines from U.S.-flag competition.

Finally, Delta states that if the Department determines to consider the application in advance of the elimination of the phase-in restrictions, the Department should carve out all of the restricted-entry markets (U.S.-Montreal/Toronto/Vancouver) from any immunity granted until the applicable phase-in restrictions expire.

### IATA

IATA requests that the Department refrain from considering in this docket the issue of whether approval of the application should affect the rights of the applicants to participate in IATA tariff coordination.<sup>31</sup> Consistent with its position in earlier antitrust cases, IATA maintains that the issue is more appropriately addressed in Docket 46928.

### Northwest

Northwest requests that the application be denied. Northwest states that the Department has firmly established a policy to consider antitrust immunity for alliances only where there is a fully effective open-skies agreement in place. Northwest maintains that the Department arguably approved the American/CAI immunity application to enhance competition with Air Canada. However, it states that awarding immunity to the United/Air Canada alliance would substantially lessen competition in the U.S.-Toronto market.<sup>32</sup>

---

<sup>31</sup> In the American/CAI immunity case, IATA recognized that the Department held open the prospect of an IATA pricing condition if future changes in the U.S.-Canada bilateral agreement “opened” fifth/sixth freedom markets, thus setting the stage for possible alliance immunity for those markets.

<sup>32</sup> Northwest notes that an attachment to Air Canada’s June 4, 1996, objection to the Department’s Show-Cause Order 96-5-38 tentatively approving the American/CAI antitrust immunity application, indicates that Air Canada has about 43% of the U.S.-Toronto market based on seats and about 50% market share based on departures.

Northwest argues that granting the application before expiration of the transitional restrictions on U.S. airlines would substantially lessen competition in the U.S.-Toronto market by further strengthening Air Canada's dominant position in that market.<sup>33</sup> Northwest also asserts that granting the application despite the U.S.-Canada bilateral agreement's significant restrictions on U.S. airline entry into the Toronto market would send a very dangerous signal to other U.S. trading partners (such as the United Kingdom) that antitrust immunity may be obtained without a full open-skies agreement.

### Joint Applicants' Replies

The Joint Applicants maintain that the objecting carriers have expended a considerable effort to show how important it is for them to increase their U.S.-Toronto services to their respective hubs. However, they have failed to show how the proposed alliance would affect their competitive presence in the Toronto city-pairs of concern. They therefore assert that the objectors have not provided a basis for depriving the public of the benefits of the United/Air Canada alliance.

As an initial matter, the applicants state that no party disputes that extensive public benefits would result from the proposed alliance. They assert that the Department has already considered and rejected the objectors' arguments regarding the characteristics of the U.S.-Canada agreement. Further, they argue that the Department has already concluded that all transborder markets except Toronto are *de facto* open to competitive entry.

Regarding the Toronto market, the Joint Applicants note that United has a relatively smaller share of the U.S.-Toronto market than does American.<sup>34</sup> They further maintain that the factors underlying a New York-Toronto "carve out" in the American/CAI case simply do not apply here given United's relatively small presence at both New York and Toronto and United's lack of any nonstop service between New York-Toronto.<sup>35</sup> As to the Chicago-Toronto market, where United and Air Canada operate overlapping nonstop service, the applicants state that it would be "fundamentally unfair" to United and Air Canada to restrict their ability to cooperate and thus to compete on an equal footing with American/CAI for Chicago-Toronto local traffic.

Moreover, they maintain that the proposed alliance will not affect consumers on those routes for which the objectors are concerned and will not upset the present competitive balance in the various Toronto markets during the Toronto phase-in period. Finally, they argue that the Department cannot lawfully grant unrestricted approval and immunity to one

---

<sup>33</sup> Northwest argues that its inability to serve Toronto from its Minneapolis hub is a perfect example of the inability of U.S. carriers to discipline Air Canada's services to Toronto.

<sup>34</sup> They claim that United has a 6.8% market share of the U.S.-Toronto market based on ASM's compared to American's 16.4%, and that United is the "fifth largest carrier" in the U.S.-Toronto market based on this market share. They also maintain that American serves more U.S. points from Toronto than any other U.S. airline (five compared to United's two).

<sup>35</sup> They further claim that United is the number four carrier in the New York/Newark market, "with a [domestic] market share of less than 8%."

alliance but not the other without adjudication of the issues in a contemporaneous carrier selection proceeding.

#### United

United also filed a separate reply in which it urges the Department to treat American's comments in this proceeding as "irrelevant" misrepresentations of United's positions in various other cases, which are without substantive merit.

### **C. Agreement Limiting Immunity**

On March 14, 1997, the Acting Assistant Attorney General of the Antitrust Division, DOJ, wrote a letter to the Assistant Secretary for Aviation and International Affairs, explaining that the DOJ and the Joint Applicants had reached an agreement on limitations on immunity in the Chicago/San Francisco-Toronto markets, and enclosing a copy of the agreed-to limitations. These limitations are contained in Appendix A.

### **IV. Tentative Decision**

We tentatively find that the Alliance Agreement should be approved and granted antitrust immunity under sections 41308 and 41309 to the extent provided below. Our examination of the Joint Applicants' proposal tentatively leads us to find that the integration of the two carriers' services will enhance competition overall and allow the airlines to provide better service and operate more efficiently. We find that it is unlikely that the Alliance Agreement, as modified by the conditions agreed upon by the applicants and the DOJ, will substantially reduce competition in any market. Finally, our approval and grant of antitrust immunity for the proposed Alliance Agreement will allow the Joint Applicants to maximize, in the U.S.-Canada transborder markets, the various pro-competitive and pro-consumer benefits that we foresaw resulting from the fundamental liberalization of air services fostered by an open aviation marketing accord.

We have tentatively determined to approve the proposed alliance because of the unique circumstances of the U.S.-Canada market. As we stated in approving the American/CAI alliance:

The U.S.-Canada relationship is *sui generis*. The two countries share the longest border in the world. The vast majority of Canadians live within an hour's flight of the American border: the resulting majority of relatively short-haul transborder markets contrast sharply with transatlantic, transpacific, and even Latin American routes. Instead of a relatively few long-range routes, many much shorter markets bind the two countries together. In addition, the volume of the bilateral market for goods and services outpaces every other international market.<sup>36</sup>

---

<sup>36</sup> Order 96-5-38 at 10.

The U.S.-Canada market is the largest international passenger market in the world, and growing rapidly. For the United States, Canada is a bilateral market in a class by itself. The U.S.-Canada transborder market supports more U.S. gateways, nonstop city-pairs, diverse airlines, and competitive routings and service options than any other international market. Perhaps most important, at the imminent conclusion of what is left of the brief phase-in of entry and capacity at Toronto, the air transport agreement between the United States and Canada will have created an open environment for all transborder passenger and belly cargo services and prices. Against this background, we tentatively find that the U.S.-Canada aviation relationship justifies positive action on the application before us, to the extent described below.<sup>37</sup>

As in the case of the American/CAI alliance, we have also tentatively decided to withhold approval and immunity from all-cargo service and from third-country markets. The U.S.-Canada aviation agreement does not provide for unrestricted all-cargo services, and does not permit unrestricted services or provide for operational flexibility in third-country markets. While we do not find these deficiencies sufficiently persuasive in the unique U.S.-Canada context to compel a negative finding on the application as a whole, we will not grant to these alliance partners immunity for cooperative activity in areas where the underlying bilateral agreement does not provide for open entry and operational flexibility immediately or subject to the short-term phase-in provisions.

We note that DOJ has raised concerns about the potential loss of competition in some particular aspects of the Chicago-Toronto and San Francisco-Toronto markets. (See pp 21-22, *infra*) The applicants have agreed to conditions designed to ameliorate DOJ's concerns in this respect--*i.e.*, the applicants have agreed to exclude coordination of specified activities relating to certain types of fares and capacity for U.S. point-of-sale local passengers flying nonstop between Chicago and San Francisco, on the one hand, and Toronto, on the other. We will adopt these conditions, which are set forth in Appendix A.<sup>38</sup>

While we have tentatively determined to approve and immunize the United/Air Canada alliance, we recognize that the competitive issues raised by this alliance proposal are different from the American/CAI alliance. We have tentatively determined to approve and immunize the United/Air Canada alliance, subject to the limitations discussed in this order, despite these considerations, because the parties opposing the application have not convinced us that the alliance, as modified by the restrictions applicable to the Chicago/San Francisco-Toronto markets, will substantially reduce competition in any

---

<sup>37</sup> No other bilateral market resembles the U.S.-Canada market and our decision here is a function of those crucial and unique circumstances, as we noted in the American/CAI decision. In other contexts, we insist upon full open-skies agreements as a prerequisite to our consideration of applications for antitrust immunity.

<sup>38</sup> We imposed similar restrictions on the American/CAI alliance in the New York-Toronto market. See Order 96-7-21 at 16.

market. The record before us does not persuade us that slot restrictions or market conditions will keep other U.S. airlines from adding or beginning service in markets served by United and Air Canada.<sup>39</sup>

We will also require the applicants (1) to file all subsidiary and subsequent agreement(s) with the Department for review;<sup>40</sup> and (2) to resubmit for review their various alliance agreement(s) in five years. We also find it in the public interest to direct Air Canada to report full-itinerary O&D Survey data for all passenger itineraries that contain a United States point (similar to the O&D data already reported by United).<sup>41</sup>

## V. Decisional Standards under 49 U.S.C. Sections 41308 and 41309

### A. Section 41308

Under 49 U.S.C. section 41308, the Department has the discretion to exempt a person affected by an agreement under section 41309 from the operations 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 by the public interest. Generally, the Department withholds antitrust immunity from agreements that do not substantially reduce or eliminate competition,<sup>42</sup> unless there is a strong showing on the record that antitrust immunity is required by the public interest, and that the parties will not proceed with the transaction absent the antitrust immunity.<sup>43</sup>

---

<sup>39</sup> See 49 U.S.C. 41309(c)(2).

<sup>40</sup> Regarding this requirement, we do not expect the alliance partners to provide the Department with the minor technical understandings that are necessary to fully blend their day-to-day operations but that have no additional substantive significance. We do, however, expect and direct the Joint Applicants to provide the Department with any agreements or other contractual instruments that may materially alter, modify or amend the Alliance Expansion Agreement. Such agreements must be reduced to writing and are not covered by immunity until and unless it is affirmatively granted. Significant implementing agreements related to the structure of the alliance must also be filed if written. If within the scope of the immunity already granted, these agreements would continue to have immunity until and unless disapproved. Contractual instruments and agreements in principal between the Joint Applicants and additional carrier partners, regardless of whether antitrust immunity is sought for any activities related to such additional partners and/or where the instruments/agreements may be drafted as separate agreements which merely supplement the “Alliance Expansion Agreement,” must also be filed for review. In such cases, the Department will determine what further action, if any, may be required with respect to such arrangements.

<sup>41</sup> We intend to use this data exclusively for purposes of monitoring the alliance. Accordingly, we will keep Air Canada’s O&D data confidential. We will not release data for Air Canada to any other carrier. Conversely, Air Canada will not gain access to O&D data for any other carrier.

<sup>42</sup> *Investigation into the Competitive Marketing of Air Transportation--Agreement Phases*, Order 82-12-85, affirmed, *Republic Airlines Inc. v. C.A.B.*, 756 F.2d 1304 (8th Cir. 1985).

<sup>43</sup> *Pan American World Airways, Inc.*, Order 88-8-18 at 9; *Investigation into the Competitive Marketing of Air Transportation--Agreement Phases*, Order 82-12-85 at 124. See 14 CFR §303.05(a) (contents of application for antitrust immunity).

## **B. Section 41309**

Under 49 U.S.C. section 41309, the Department must determine, among other things, that an intercarrier agreement is not adverse to the public interest and not in violation of the statute before granting approval.<sup>44</sup> The Department cannot approve an intercarrier agreement that substantially reduces or eliminates competition unless the agreement is necessary to meet a serious transportation need or to achieve important public benefits that cannot be met, and those benefits cannot be achieved, by reasonably available alternatives that are materially less anticompetitive.<sup>45</sup> The public benefits include international comity and foreign policy considerations.<sup>46</sup>

The party opposing the agreement or request has the burden of proving that the agreement substantially reduces or eliminates competition and that less anticompetitive alternatives are available.<sup>47</sup> On the other hand, the party defending the agreement or request has the burden of proving the transportation need or public benefits.<sup>48</sup>

## **VI. Tentative Approval of the Agreement**

### **A. Excluded Services**

It is the Department's policy not to approve and grant antitrust immunity to international inter-carrier cooperation agreements in markets that lack complete freedom of operation for international services. Accordingly, consistent with our rulings in the *American/CAI* case, we have tentatively determined to withhold approval and immunity for the following services and markets: (1) third-country (fifth- and sixth-freedom) markets and (2) all-cargo services. We will also exclude matters relating to fares and capacity for particular categories of U.S. point-of-sale local passengers in the Chicago- and San Francisco-Toronto markets, as agreed between the Joint Applicants and DOJ.

#### **1. Third-Country Fifth- and Sixth-Freedom Markets**

We estimate that the alliance could provide new or additional on-line connecting service in over 4,000 city-pair markets from 231 U.S. cities served by United to 18 transatlantic and transpacific cities served by Air Canada. These markets accounted for 19.5 million O&D passengers during 1995.<sup>49</sup> In addition, the alliance could also provide new on-line service

---

<sup>44</sup> Section 41309(b).

<sup>45</sup> Section 41309(b)(1)(A) and (B).

<sup>46</sup> Section 41309(b)(1)(A).

<sup>47</sup> Section 41309(c)(2).

<sup>48</sup> *Id.*

<sup>49</sup> Our analysis is based on the Origin-Destination Survey of Airline Passenger Traffic for 1995, adjusted to account for traffic carried by non-reporting foreign airlines, based upon T-100 and T-100(f) international segment and market data (Data Banks 28-IS and 28-IM). We have determined that the

in nearly 8,000 markets between 69 Canadian cities served by Air Canada and the 113 transatlantic, transpacific, and Latin American cities served by United.

As we indicated in approving the American/CAI alliance, we tentatively conclude that we should deny approval and antitrust immunity to third-country markets, notwithstanding the large potential traffic flows in the third-country markets, inasmuch as these markets are not open to code-sharing by competing carriers. Except for the U.S., the Canadian government's aviation agreements with other countries generally provide for only limited entry. The U.S.-Canada aviation agreement does not provide for third-country code-sharing operations or for fifth-freedom rights, and sixth-freedom operations are subject to a mandatory change of flight number at the homeland gateway. As a consequence, we concluded in the American/CAI case that other U.S. carriers and alliances -- either in partnership with other Canadian carriers or with third-country carriers -- would have little opportunity to compete with the American/CAI alliance in third-country markets. We find that these considerations apply with equal force in the case of the proposed United/Air Canada alliance.

In view of the foregoing reasons, we tentatively conclude that the restrictions applicable to third-country markets are not consistent with our policy of granting antitrust immunity only in open competitive markets and will deny approval and withhold antitrust immunity from the alliance in third-country markets.<sup>50</sup> As we stated in the American/CAI case, however, if the Canadian government were to agree to amend the U.S.-Canada aviation agreement to grant mutual fifth-freedom and third-country code-sharing rights, we would then consider extending immunity to third-country markets.

## 2. All-Cargo Services

The Joint Applicants also propose to coordinate and integrate their cargo service including scheduling, pricing, and marketing. However, the new U.S.-Canada aviation agreement precludes co-terminalization in the other party's territory for all-cargo service (except with aircraft having a maximum certificated takeoff weight less than 35,000 pounds). This restriction effectively precludes the operation of all-cargo service making multiple stops in the other country's territory. The proposed alliance would be able to avoid this restriction through cooperative all-cargo operations, and as such would have significant competitive advantages over other airlines offering all-cargo service. Accordingly, as in the case of the American/CAI alliance, we have tentatively determined to deny approval and withhold

---

public interest warrants our use of and limited disclosure of such data in this proceeding, because the public interest in evaluating this application on the basis of these data clearly outweighs any possible competitive disadvantage U.S. carriers might face from release of these data to foreign carriers. This determination is consistent with (1) the requirements set forth in sections 19-6(b) and 19-7(d) and (e) of 14 CFR Part 241 as they pertain to international T-100/T-100(f) data and O&D data, respectively, and (2) the Department's policy statement set forth in 14 CFR section 399.100, which provides that the Department may disclose restricted O&D data consistent with its regulatory functions and responsibilities.

<sup>50</sup> See Order 96-7-21.

antitrust immunity for all-cargo services.<sup>51</sup> Were the Canadian government to reconsider opening up all-cargo markets, we would give favorable consideration to requests for approval and immunity for all-cargo service.

## B. Inclusion of Toronto Markets

One troubling aspect of the Toronto markets affected by the application is the continuing limitation on U.S.-flag entry in the U.S.-Toronto market until February 1998. As in the case of the American/CAI alliance, therefore, we have carefully considered whether we should withhold our approval and grant of antitrust immunity on public interest grounds for all alliance services to Toronto, where restrictions remain under the U.S.-Canada agreement.<sup>52</sup> As already noted, we explored at length the peculiarities of the Canadian market in the American/CAI case.<sup>53</sup> As in that case, we have tentatively concluded, nevertheless, that despite our policy not to grant antitrust immunity in markets where there are significant restrictions on entry or flexibility of operations, the unique circumstances of the U.S.-Canada Agreement; the limited nature and very short duration of the continuing restrictions; and the significant consumer competitive advantages that will arise from this alliance justify our grant of approval and immunity in these markets, notwithstanding the restrictions temporarily in effect.

Accordingly, considering that the alliance, as modified by the agreement between the Joint Applicants and the DOJ, will not adversely affect competition to any significant degree, and in view of the special features or characteristics applicable to the U.S.-Canada market, we tentatively find it unnecessary otherwise to withhold approval and immunity in the Toronto markets.

Considering all these factors and the substantial consumer benefits to be derived from the alliance during this period,<sup>54</sup> we are tentatively persuaded that, under these unique circumstances, the public interest does not require that we withhold approval and immunity for operations in this temporarily restricted market.

Our tentative decision to afford antitrust immunity prior to the complete *de jure* opening of the Toronto market is based on a determination that delaying the effectiveness of immunity would serve no significant public interest purpose. First, we anticipate that the additional route opportunities<sup>55</sup> made available in February 1997 will come near to satisfying U.S.-carrier demand for access to that market. Second, we rely on the fact that,

---

<sup>51</sup> Our withholding approval and immunity for all-cargo service does not apply to belly freight service on combination aircraft, where similar bilateral restrictions do not apply.

<sup>52</sup> As discussed below, pp. 25-26, we have tentatively determined that this alliance is not likely to reduce substantially competition in U.S.-Toronto markets based on the alliance agreement as modified by the conditions agreed upon by the Joint Applicants and the DOJ.

<sup>53</sup> See pp. 13-14, *supra*.

<sup>54</sup> See, e.g., pp. 20-21, *infra* (discussion of procompetitive benefits).

<sup>55</sup> Order 97-4-4.

under the U.S.-Canada bilateral, open skies will become effective in February 1998 automatically without any further action by any government entity. Absent this automaticity and short period, we would not grant immunity for the U.S.-Toronto routes.<sup>56</sup>

While tentatively deciding to afford immunity for the U.S.-Toronto routes (other than as to specified U.S.-originating traffic for Chicago and San Francisco), this does not represent a relaxation of our policy regarding antitrust immunity; rather, as in American/CAI, it represents a temporary and exceptional adaptation of that policy in the unique U.S.-Canada circumstances. To be entirely clear, our policy is to consider the grant of antitrust immunity only where the market(s) at issue are fully open to new entry and operations -- both *de jure* (by reason of bilateral agreements) and *de facto*. Only in such markets can we be assured that immunity will be pro-competitive and pro-consumer, the touchstones of our immunity approach. Moreover, it must be clearly understood that the existence of an open skies relationship in no way "guarantees" any grant of immunity. To the contrary, it is entirely possible that immunity will not be found to be pro-competitive or pro-consumer in particular cases notwithstanding a fully open national market depending on such factors as relevant market concentration, potential future barriers, overall dominance, size of the applicants, and the like. In short, an open skies agreement, even where it is also a *de facto* open entry market, is a necessary, but not sufficient basis for the grant of antitrust immunity.

### C. Antitrust Issues

The Joint Applicants state that through the Alliance Agreement they intend to broaden and deepen their cooperation in order to improve efficiency, expand various benefits available to the traveling and shipping public, and enhance their ability to compete in the global marketplace. They state that, while retaining their separate corporate and national identities, they fully intend to cooperate to the extent necessary to create a seamless air transport system. Accordingly, the Alliance Expansion Agreement's intended commercial and business effects are equivalent to a merger of the two airlines.

In determining whether the proposed transaction would violate the antitrust laws, we will apply the standard Clayton Act test used in examining whether mergers will substantially reduce competition in any relevant market.<sup>57</sup>

The Clayton Act test requires the Department to consider whether the Agreement will substantially reduce competition by eliminating actual or potential competition between United and Air Canada so that they would be able to effect supra-competitive pricing or

---

<sup>56</sup> We also note that the Joint Applicants have accepted certain limitations and conditions to their alliance agreement equivalent to those imposed by the DOJ on the earlier approved American and CAI arrangement. Order 96-7-21.

<sup>57</sup> Order 92-11-27 at 13.

reduce service below competitive levels.<sup>58</sup> To determine whether a merger or comparable transaction is likely to violate the Clayton Act, the DOJ and the Federal Trade Commission (“FTC”) use their published merger guidelines.<sup>59</sup> The Merger Guidelines' general approach is that transactions should be blocked if they are likely to create or enhance market power. Market power is defined as the ability profitably to maintain prices above competitive levels for a significant period of time (firms with market power can also harm customers by reducing product and service quality below competitive levels). To determine whether a proposed merger is likely to create or enhance market power, the DOJ and the FTC primarily consider whether the merger would significantly increase concentration in the relevant markets, whether the merger 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 the merger's potential for harm.

On such antitrust issues we consult with the DOJ, given its experience and responsibility for the enforcement of the antitrust laws. In reaching our public interest determinations in these cases, we fully consider and give weight to DOJ's concerns and recommendations.

### **1. The Alliance's Procompetitive Benefits**

The traditional analysis for airline mergers has focused on discrete city-pair routes. Without minimizing the significance of city-pair analysis, however, we believe it also important to recognize that the rapid growth and development of international airline alliance networks requires an additional perspective on competitive impact -- the perspective of more broadly defined open aviation markets (in this case, the U.S.-Canada transborder market) in which travelers have multiple competing options for reaching destinations over multiple intermediate points. The pro-competitive effects of such alliances can be particularly evident in the case of markets between points lying behind the U.S. gateway and points lying beyond the Canadian gateway where integrated alliances with coordinated connections, marketing, and services can offer competition well beyond mere interlining. The competitive effect is also evident, albeit less dramatic than in transatlantic markets, in the case of services between interior U.S. cities and Canadian gateways, or between U.S. gateways and interior Canadian cities. These types of alliances, as a result of their increased operational integration, can better offer a multitude of attractive new on-line services to thousands of U.S.-Canada transborder city-pair markets. Thus, a significant element in antitrust analysis is the extent to which facilitating airline integration (through antitrust immunity or otherwise) can enhance overall competitive conditions.

Our analysis indicates that this alliance will have a strong pro-competitive impact, bringing on-line service to nearly 16,000 transborder city-pair markets with an estimated traffic of nearly 9 million passengers. In particular, the alliance will significantly increase

---

<sup>58</sup> See Order 96-5-38 at 16.

<sup>59</sup> 57 Fed. Reg. 41552 (September 10, 1992).

competition and service opportunities for many of the 4.5 million U.S.-Canada passengers in behind-U.S. gateway and beyond-Canadian gateway markets, by offering the equivalent of new on-line service in many of these city-pair markets that are not now served by either party alone.<sup>60</sup> This analysis further supports our belief that these alliances will benefit consumers by increasing U.S.-Canada service options and enhancing competition between airlines, particularly for traffic to or from cities behind or beyond major gateways for transborder service. U.S. consumers and airlines should be major beneficiaries of this expansion and the associated increase in service opportunities.

Furthermore, as a general rule airlines, like other firms, may engage in joint ventures and cooperative arrangements without violating the antitrust laws. The courts and the enforcement agencies have usually found that such arrangements are likely to promote economic efficiency and further competition.<sup>61</sup> As discussed above, that has been our experience with the Northwest/KLM alliance--the integration of those partners' operations has increased the efficiency of their operations and made it possible for the two carriers to offer improved service.

## 2. The Justice Department's Review

DOJ has examined the likely competitive impact of the proposed alliance between United and Air Canada. DOJ identified two nonstop markets -- Chicago-Toronto and San Francisco-Toronto -- where it was concerned that competition could be reduced if United and Air Canada were authorized to agree on fares and capacity for local traffic. After discussions between the DOJ and the applicants, the applicants have agreed to limit the scope of their requested immunity so as to exclude certain activities relating to particular fares and capacity for U.S. point-of-sale local passengers on the Chicago-Toronto and San Francisco-Toronto routes.

The conditions agreed upon by DOJ and the applicants are attached as Appendix A to this order. In brief, the restrictions are designed to preserve competition for *all* local nonstop fares in the Chicago-Toronto market and all *unrestricted* local nonstop fares in the San Francisco-Toronto market. Specifically, the agreement would exclude from the grant of immunity the following activities: pricing, inventory or yield management coordination, or pooling of revenues, with respect to local U.S. point-of-sale passengers flying nonstop between Chicago/San Francisco and Toronto, with certain exceptions. The exceptions that would be covered by antitrust immunity would be the promotion and sale of certain discounted fare products: corporate fares, consolidator and wholesaler fares, promotional fares, group fares, and fares for government traffic or other traffic that either party is prohibited by law from carrying on services operated under its own code. (These exceptions are subject to limitations designed to preserve competition for local passengers.

---

<sup>60</sup> Combined Transborder Origin-Destination Survey (Data Bank 9), Calendar Year 1995.

<sup>61</sup> See, e.g., *Northwest Wholesale Stationers v. Pacific Stationery & Printing Co.*, 472 U.S. 284, 295 (1985).

For example, coordination on certain kinds of promotional fare products would be immunized only if they are offered in at least 25 other city-pair markets, and corporate and group fare products would not receive immunity if they exceeded 25 percent of a corporation's or group's anticipated travel.) In addition, "restricted" fares<sup>62</sup> for local U.S.-point-of-sale passengers flying nonstop between San Francisco and Toronto would be exempt from the limitations on immunity. The agreement also provides for the Department to review the continuing need for the limitations on immunity within eighteen months of a final order or on application of the Joint Applicants.

Accordingly, we will exclude the foregoing fares, service, and activities--as agreed to by the Joint Applicants and DOJ--from our grant of immunity. Our antitrust analysis, *infra*, reflects that exclusion.

### **3. Other Markets Affected by the Application**

In addition to considerations of general transborder airline network competition (and after excluding all-cargo services, and third-country fifth- and sixth-freedom markets), there are three relevant types of markets requiring a competition analysis: first, the aggregate U.S.-Canada market; second, the individual city-pair markets; and last, the behind- and beyond-gateway transborder markets.

#### **(a) The U.S.-Canada Market**

We have tentatively determined that the Alliance Agreements, as conditioned, will not significantly reduce competition in the aggregate U.S.-Canada transborder market. During the 12 months ending September 1996, our analysis shows that United's U.S.-Canada scheduled nonstop passenger share was 7.3 percent and Air Canada's scheduled nonstop passenger share was 24.4 percent. The Joint Applicants' combined share of the market was 31.7 percent. During the same period, American had a 16.0 percent market share and CAI had 9.1 percent, for a total of 25.2 percent. In addition, Delta carried about 12 percent of transborder passengers, Northwest 11 percent, and US Airways 6 percent, and several other U.S. and Canadian carriers had market shares between 0.5 percent and 4.9 percent.<sup>63</sup> The Herfindahl-Hirschman Index (HHI)<sup>64</sup> was 1,703 (counting

---

<sup>62</sup> Restricted fares require either a Saturday night stay or a minimum advance purchase of at least seven days.

<sup>63</sup> T-100 and T-100(f) nonstop segment data (Data Bank 28-IS).

<sup>64</sup> The Herfindahl-Hirschman Index is a measure of market concentration. It is computed by adding the square of each firm's percentage market share. Thus, a monopoly market would have an HHI of 10,000 (100\*100), a market with two firms of equal size would have an HHI of 5,000 (50\*50\*2), and a market with 10 firms of equal size would have an HHI of 1,000 (10\*10\*10). Generally speaking, DOJ considers markets with HHI under 1,000 to be unconcentrated, markets with HHI between 1,000 and 1,800 to be moderately concentrated, and markets with HHI greater than 1,800 to be highly concentrated.

the American/CAI alliance as one carrier). The proposed United/Air Canada alliance would increase nonstop passenger HHI by 381 points, to 2,084.<sup>65</sup>

Similarly, during Calendar Year 1995, Air Canada had a 29 percent share of true transborder O&D passengers, and United had 9 percent, for a proposed alliance total of 38 percent. In comparison, the American/CAI alliance carried 22 percent of true U.S.-Canada O&D passengers (17 percent for American and 5 percent for CAI). In addition, Delta had a 16 percent O&D share, Northwest 12 percent, and US Airways nine percent. Calendar Year 1995 HHI for true U.S.-Canada O&D passengers (counting the American/CAI alliance as one carrier) was 1,853. The proposed alliance would produce an overall HHI of 2,381, an increase of 528 points.

Importantly, we expect that the ability of other airlines to increase or begin service in U.S.-Canada markets should restrain the Joint Applicants from charging supracompetitive fares or reducing service below competitive levels. However, the United/Air Canada proposal would fail traditional merger guidelines, due to the increase in the HHI. Nonetheless, this increased concentration must be considered in the context of the application as modified by the agreement between the Joint Applicants and the DOJ on immunity in the Chicago-Toronto and San Francisco-Toronto markets, the first and tenth-largest transborder markets, respectively. As a consequence, we tentatively conclude that the application as modified by the agreement between the Joint Applicants and the DOJ for the Chicago and San Francisco-Toronto markets will not significantly reduce competition in the overall U.S.-Canada market.

The elimination of most restrictions on new and increased U.S. carrier services has already dramatically changed U.S.-Canada markets and resulted in a large growth of new transborder service. During 1996, there were 15.5 million transborder passengers, an increase of 28 percent from the 12.1 million in 1994. As of December 1996, U.S. and Canadian carriers together provided nonstop service in 73 nonstop markets with more than 50,000 annual passengers, compared to only 54 in 1994, and there were 22 markets with bilateral nonstop competitive service (at least one flag carrier of each nation). Of the top 50 U.S.-Canada city-pair markets, 17 have gained their first nonstop service since signing of the new U.S.-Canada agreement. Passenger fares in the 50 top transborder markets have declined an average of 22 percent since 1994, and in the 17 top-50 markets that have gained their first nonstop service, average fares have declined 32 percent. Furthermore, since 1994 17 U.S. cities have gained their first nonstop scheduled service to Canada.<sup>66</sup> This growth can be directly attributed to the new bilateral agreement's elimination of governmental restraints on entry in the U.S.-Canada transborder market. Given our experience since the removal of restrictions on entry, we believe that the HHI

---

<sup>65</sup> We also must consider the competitive effects of the United/Air Canada alliance in light of the current situation in the relevant markets, which includes the existence of the alliance between American and CAI, the only Canadian airline besides Air Canada of significant size.

<sup>66</sup> Office of International Aviation, *The Impact of the New US-Canada Aviation Agreement At Its Second Anniversary*, April 1997.

ratios do not accurately reflect the likely competitive effect of the United/Air Canada alliance.

### **(b) The City-Pair Markets**

The alliance will directly affect competition in the five nonstop markets where United and Air Canada both operate flights and in the eleven nonstop markets where they compete through code sharing, even though all of the flights in each of those markets are operated either by Air Canada or by United, not by both. (See page 4, *supra*.) As discussed above, the applicants have undertaken to exclude from the scope of requested immunity capacity, fares, and yield management decisions for certain categories of U.S.-source local passengers in the Chicago- and San Francisco-Toronto markets.

We note that concentration figures in individual city-pair markets are not conclusive. Individual airline nonstop city-pair markets usually have high levels of concentration, since most nonstop markets are served by only a few airlines. The key consideration for determining whether the United-Air Canada alliance (or any other airline merger or joint venture) is likely substantially to reduce competition is potential competition (*i.e.*, whether other airlines can enter the relevant markets in response to inadequate service or supra-competitive prices) including one-stop and connecting competition.<sup>67</sup> The new aviation agreement with Canada will soon eliminate all governmental restrictions on entry into U.S.-Canada transborder markets for U.S. and Canadian airlines. The agreement will accordingly eliminate the most significant barrier to entry in those markets. The relevant considerations here, then, are whether other factors will prevent U.S. and foreign airlines from entering U.S.-Canada markets, should the applicants increase fares above, or lower service below, competitive levels.

We conclude that the alliance is unlikely to cause a significant reduction in competition in any of the overlap nonstop markets where we have tentatively decided to grant immunity: Los Angeles/San Francisco-Vancouver and San Francisco-Calgary.

In the Los Angeles-Vancouver market, Air Canada's market share was only 15 percent and United's less than 7 percent, for a combined alliance total of only 22 percent. The dominant carrier in this market was CAI which carried nearly 43 percent of nonstop passengers. In addition, Delta had a market share of 28 percent and Canada 3000 (a Canadian airline) had an 8 percent share.<sup>68</sup>

---

<sup>67</sup> The Department has tentatively taken the view that, for a large number of travelers in long-haul markets not constrained by strict time-sensitivity, one-stop and connecting service can provide a reasonable substitute for nonstop service and should be considered as a competitive option for purposes of antitrust analysis. (See Order 96-5-12 at 23 n.50.)

<sup>68</sup> T-100 and T-100(f) data (Data Banks 28-IS and 28-IM).

United was the largest carrier in the San Francisco-Vancouver market with 39 percent of nonstop passengers, while Air Canada carried 18 percent for an alliance total of 58 percent. In addition, CAI had a 29 percent market share, and Delta 13 percent.

The San Francisco-Calgary market was divided nearly equally between Air Canada, which carried 46 percent of the nonstop passengers, and United, which had a market share of 54 percent. Together, the proposed alliance had a 99.7 percent share.

None of these three nonstop city-pair markets involves a hub dominated by one of the applicants.<sup>69</sup> The Joint Applicants will also continue to face significant nonstop competition in the Vancouver-Los Angeles/San Francisco markets, as well as significant connecting competitive service. Most importantly, with the exception of U.S.-Toronto markets, all U.S.-Canada markets are now open to unlimited entry by U.S. and Canadian carriers. Together, all these factors should assure that the proposed alliance will not enable the Joint Applicants to raise fares above (or reduce service below) competitive levels. We tentatively conclude, therefore, that the proposed alliance will not have a significant adverse effect on competition in these markets.

We have focused on the alliance's likely competitive effect in the nonstop markets where the applicants currently compete with each other. While the United/Air Canada alliance will also affect competition in U.S.-Canada markets where the applicants compete by offering connecting service or one-stop service, we doubt that the transaction will have any significant impact in such markets. Passengers who travel in U.S.-Canada markets where no nonstop service is available, or who take connecting service even though nonstop service is available, should be able to choose between services offered by several carriers. The United/Air Canada alliance should not give the applicants market power in any such markets.

### **(c) Toronto Markets**

Toronto markets may be a concern. Air Canada is by far the largest carrier at Toronto where it operated 43 percent of Toronto-U.S. departures during the 12 months ending September 1996 and enplaned 39 percent of Toronto-U.S. passengers. With its partner United, Air Canada had about a 48 percent share of Toronto-U.S. departures and about a 46 percent share of Toronto-U.S. passengers. Its nearest competitor, CAI, had only about 10 percent of Toronto-U.S. departures and 9 percent of Toronto-U.S. passengers.

---

<sup>69</sup> Vancouver, in fact, is the principal hub of CAI, Air Canada's principal competitor. In addition, although United operates a hub at San Francisco, where it is the largest carrier, with about 57 percent of domestic departures and passengers, and about 55 percent of total passengers and departures, the carrier's hub operations are primarily for United's transpacific operations. United's strength at San Francisco accordingly should not prevent entry or increased service by competing airlines. There are also no capacity constraints such as slot controls at San Francisco to inhibit new competitive service.

Together, the competing American/CAI alliance had a 26 percent share of Toronto-U.S. departures and about a 28 percent share of Toronto-U.S. passengers.<sup>70</sup>

Toronto is Air Canada's hub and the most important origin point for Canadian airline travelers and the most important destination for U.S. airline travelers. Toronto's airport, moreover, has slot restrictions which may limit an airline's ability to begin or increase service in Toronto markets.

Continental has raised the issue of the potential scarcity of competitive slots at Toronto for U.S. airlines wishing to expand or initiate service between Toronto and U.S. gateways. We believe that *de facto* access to airports is a critical element in evaluating applications for antitrust immunity, and we are not prepared to grant immunity where U.S. carriers are effectively precluded from competitive entry because of slot constraints.

Nevertheless, we have tentatively determined to approve and immunize the United and Air Canada alliance, because the record does not show that the alliance as conditioned is likely to reduce substantially competition at Toronto. Insofar as U.S.-originating local traffic is concerned, the Chicago-Toronto and San Francisco-Toronto markets are largely excluded from our grant of immunity as a result of the Joint Applicants' agreement with the DOJ. The Joint Applicants do not now operate competing flights in any other Toronto nonstop market, and only two of the overlap markets served by code-sharing are Toronto markets (Los Angeles-Toronto and Washington-Toronto).<sup>71</sup>

Moreover, the competitive significance of current market shares and potential slot constraints is lessened by several features. The agreement between the Joint Applicants and the DOJ limits antitrust immunity with respect to the Chicago-Toronto and San Francisco-Toronto markets, thus ensuring continued competition for most local traffic in those markets. To the extent that Toronto is a significant connecting point for other destinations in Canada, such destinations will be subject to competition and the discipline of market forces through other gateways and, in many cases, through their own nonstop services to U.S. points. Still more significant is the presence of many U.S. carriers at Toronto already, even though that presence may be, in individual cases, briefly limited by the terms of the bilateral.

Furthermore, Continental has not shown that the slot restrictions at Toronto have prevented it from operating services that it is authorized to provide or that they are likely to prevent new service in the future. Given this state of the record, we could not find that the opponents have met their burden of proof of showing that approval and immunity will substantially reduce competition.

---

<sup>70</sup> T-100 and T-100(f) nonstop and market data (Data Banks 28-IS and 28-IM; specifically, enplaned passengers).

<sup>71</sup> Moreover, with respect to operations prior to February 24, 1998, the alliance will continue to be subject to the restrictions on code shares applicable under the U.S.-Canada Agreement (Annex V, temporary Section 4) at Toronto. These restrictions limit the number of gateway-to-gateway transborder flights on which passengers to/from U.S. points beyond/behind the U.S. gateway may be carried, given the limited number of new opportunities at Toronto available to U.S. carriers.

**(d) The Behind- and Beyond-Gateway Transborder Markets**

As we noted above, the pro-competitive effects of global alliances can be particularly evident in the case of the behind- and beyond-gateway markets where many passengers now lack convenient on-line service. The proposed alliance would result in enhanced on-line connecting opportunities in nearly 16,000 city-pair markets from 231 U.S. cities to 69 cities in Canada. Accordingly, we tentatively conclude that the proposed alliance will significantly increase competition in the behind- and beyond-gateway U.S.-Canada markets.

Except as provided above, we tentatively find that the Agreement will substantially benefit competition, subject to the conditions stated by this order, since it will enable the Joint Applicants to operate more efficiently, provide the public with a wider variety of on-line services, and permit United and Air Canada to compete more effectively with the other transborder alliance. Therefore, we tentatively find that the proposed Alliance Agreement, as conditioned, will not cause a substantial reduction or elimination of competition.

**D. Public Interest Issues**

Under section 41309, we must determine whether the Alliance Agreement would be adverse to the public interest. A similar public interest examination is required by section 41308. Except as noted, we tentatively find that approval of the Alliance Agreement will promote the public interest.

Subject to the remaining phase-in provisions for Toronto, which soon expire, the open transborder agreement with Canada gives any authorized carrier from either country the ability to serve any route between the two countries (including open intermediate and beyond transborder rights) if it so wishes. With the exceptions noted, the agreement places no limits on the number of flights that can be operated, and carriers can charge any fare unless it is disapproved by both countries.

Except as provided above with respect to all-cargo services and third-country fifth- and sixth-freedom markets, we tentatively find that the Alliance Agreement, as modified by the agreement between the Joint Applicants and the DOJ, is likely to benefit the traveling public in numerous markets and is unlikely to reduce competition materially.

In this case, having tentatively determined that the overall competitive effect of the Alliance Expansion Agreement is beneficial and consistent with our international aviation policy, we believe that the public interest favors approval of the agreement and the grant of antitrust immunity. In so stating, of course, we will continue to monitor closely the effects of an immunized alliance on consumers and on competition, to ensure that the

---

<sup>72</sup> T-100 and T-100(f) nonstop and market data (Data Banks 28-IS and 28-IM).

immunized alliance continues to serve the public interest, and will review the entire agreement in five years.

## **VII. 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 the 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. We are willing, however, to grant immunity if the parties to such an agreement would not otherwise go forward, and if we find that grant of antitrust immunity is required by the public interest.

The Joint Applicants operate competing flights in five nonstop transborder markets. In addition, the current code-share arrangements between the Joint Applicants involve fifteen gateway-to-gateway nonstop transborder routes and several one-stop transborder routes.<sup>73</sup> Consequently, the Joint Applicants are also actual or potential competitors with each other on all their code-sharing routes and are thus potentially exposed to hostile litigation under the antitrust laws.

United and Air Canada have categorically stated that they will not proceed with the Alliance Expansion Agreement without antitrust immunity. The Joint Applicants maintain that the public benefits they seek to achieve through the formation of an expanded alliance cannot be accomplished absent antitrust immunity. They claim that the proposed integration of services will expose them to unacceptable antitrust risk. The full operational integration planned by the Joint Applicants will necessarily mean that they will coordinate all of their U.S.-Canada business activities including scheduling, route planning, pricing, marketing, sales, and inventory control.

Since the antitrust laws allow competitors to engage in joint ventures that are pro-competitive, we think it unlikely that the integration of the applicants' services in the manner here approved would be found to violate the antitrust laws.<sup>74</sup> Nevertheless, since the applicants will be ending their competitive service in some markets, they could be subjected to antitrust litigation if we did not grant immunity. We are also persuaded that they will not proceed without it.

To the extent discussed above, we tentatively find that antitrust immunity should be granted to the Alliance Agreement. If we decide to approve and immunize it, we also intend to review and monitor the applicants' progress in implementing the Agreement to ensure that the applicants are carrying out the Agreement's pro-competitive aims. We propose to require the Joint Applicants to resubmit the Agreement for review in five years.

---

<sup>73</sup> United and Air Canada do not hold authority to code-share to third countries.

<sup>74</sup> Cooperative arrangements between airlines are today commonplace. We are unaware of any holding that such arrangements violate the antitrust laws. Order 92-11-27 at 19.

### **VIII. IATA Tariff Coordination Issue**

As we did in the American/CAI case, we have tentatively decided not to condition our grant of antitrust immunity to the Alliance upon the withdrawal by the Joint Applicants from IATA tariff coordination activities.<sup>75</sup> We believe that this condition is unnecessary. Since we tentatively propose to limit our grant of immunity in this case to transborder U.S.-Canada markets, and since there is no IATA traffic conference for U.S.-Canada markets, the proposed alliance, as conditioned, raises no prospects of the overlapping "dual" immunity that troubled us in the United/Lufthansa, United/SAS, and Delta/Austrian/Sabena/Swissair alliances, and we see no need here to impose any conditions on IATA participation.

In the event, however, that future talks between the Governments of the United States and Canada result in further liberalization of the U.S.-Canada aviation agreement to provide for fifth- and sixth-freedom route rights and third-country code-shares, we would expect to impose limitations (similar to those we adopted in the above cited cases) on the alliance's participation in IATA tariff conferences as a condition for granting immunity to third-country code-share operations.

### **IX. O&D Survey Data Reporting Requirement<sup>76</sup>**

We have access to market data where our carriers operate, including markets that they serve jointly with foreign airlines, such as, 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 for three 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.

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 ensure that our grant of antitrust immunity does not lead to anticompetitive consequences. We have therefore tentatively decided to require foreign airline partners of our carriers in alliances with antitrust immunity to report full-itinerary Origin-Destination

---

<sup>75</sup> We decided to place conditions on IATA tariff conference participation on the United/Lufthansa alliance in Order 96-5-27, the Delta/Austrian/Sabena/Swissair alliance in Order 96-6-33, and the United/SAS alliance in Order 96-11-1.

<sup>76</sup> 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 monitoring purposes, we will not disclose it to any other airlines.

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 United).<sup>77</sup>

We note that Air Canada already reports this data to the Canadian government which, pursuant to an informal intergovernmental agreement between the Department of Transportation and the Canadian Ministry of Transport, exchanges U.S.-Canada O&D data with the Department. As a practical result, therefore, Air Canada is already indirectly providing us with its O&D data. Under the current system, however, Air Canada is under no compulsory obligation to provide this data to us. By requiring Air Canada to file directly, we will have the ability to ensure that Air Canada provides timely, accurate data.

To prevent this reporting requirement from having any anticompetitive consequences, we will grant confidentiality to Air Canada's Origin-Destination report and special report 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 air carriers 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).

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 found it appropriate to direct Air Canada to provide certain limited Origin-Destination data to the O&D Survey, Air Canada is not an air carrier within the meaning of Part 241. 14 C.F.R. Part 241, section 3 defines an air carrier as "[a]ny citizen of the United States who undertakes, whether directly or indirectly or by a lease or any other arrangement, to engage in air transportation." Air Canada accordingly will have no access to the data filed by U.S. air carriers. Moreover, we are making Air Canada's submissions confidential while maintaining the current restriction on access to U.S. air carrier Origin-Destination data by foreign air carriers.

---

<sup>77</sup> We intend to request other foreign carrier members of international alliances involving U.S. carriers to submit O&D Survey data and condition any further grants or renewals of antitrust immunity on provision of such data.

## **X. Operation under a Common Name/Consumer Issues**

Since operation of the Alliance Agreement 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 carriers to be unfair and deceptive and in violation of the Act, unless the airlines give reasonable and timely notice of its existence.<sup>78</sup>

## **XI. Star Alliance**

On May 14, 1997, the Joint Applicants and four other airlines announced the formation of the “Star Alliance”, which is composed of United Airlines, Air Canada, Lufthansa German Airlines, Scandinavian Airlines System, Thai Airways International, and (in October 1997) Varig Brazilian Airlines. The Star Alliance participants have signed a non-binding memorandum of intent to coordinate many of their marketing and some of their operational activities on a worldwide basis. United and Air Canada have not filed any description of the proposed Star Alliance arrangements in this docket.

The Star Alliance involves matters relevant to our assessment of the competitive implications that we have been addressing in this case. To enable us to consider the Star Alliance’s potential impact on the United/Air Canada Alliance, we are directing United and Air Canada to provide within seven days of the service date of this order (1) a detailed explanation of the content, scope and timing of the Star Alliance and how the six participants will be integrated; (2) complete information (including copies of commercial agreements in final, or in draft if there is no final) on the Star Alliance, particularly on its role in the proposed United/Air Canada alliance, in terms of corporate strategy, marketing, yield and capacity management, and pricing; and (3) complete information on the extent to which the Star Alliance would affect operations between the U.S. and Canada by United or Air Canada with respect to passengers with an origin or destination in third countries. We will give interested parties 21 days thereafter to file answers to both this order to show cause and the information provided by the Joint Applicants concerning the Star Alliance.

By proceeding in this fashion, we are able to give full consideration to recent developments which could have an impact on the competitive analysis of the proposed United/Air Canada alliance. This action will allow us and interested parties an opportunity to examine record evidence on the Star Alliance before comments on this show cause order are submitted. We will then consider views of parties on that new evidence along with their views on this order to show cause and the record material already filed. Should we decide upon a review of the Star Alliance information submitted and any comments on it, that our tentative decision requires modification, we will provide for such additional procedures as may be appropriate before reaching a final decision on the record.

---

<sup>78</sup> See 14 C.F.R. §399.88.

## **XII. Summary**

We tentatively conclude that granting the application for approval and antitrust immunity for the Alliance Expansion Agreement will benefit the public interest by enhancing service options available to travelers, benefiting U.S. consumers, and encouraging a further liberalization of the transborder and global marketplace. We believe that the Alliance Agreement will strengthen competition in the markets that the applicants serve, since it will enable them to offer better service and to operate more efficiently.

We tentatively conclude that our grant of approval and antitrust immunity to the Alliance Expansion Agreement should be conditioned, as set forth in this order. We also tentatively direct United and Air Canada to resubmit the pertinent Alliance Agreement five years from the date of the issuance of the final order in this case. However, the Department is not authorizing the Joint Applicants to operate under a common name or use common brands. If the Joint Applicants wish to operate under a common name or brands, they will have to comply with our relevant procedures before implementing the change.

In addition, to the extent not otherwise limited by our conditions and limitations, we tentatively limit and condition, as delineated in subparagraphs (a), (b), and (c) to ordering paragraph 1 and in Appendix A of this order, the Joint Applicants' request regarding their proposed integration of services and operations between points in the United States and Canada. We also tentatively direct the Joint Applicants to file all subsidiary and/or subsequent agreement(s) with the Department for prior approval, and we tentatively direct Air Canada 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 United).

Before reaching a final decision, the Department will consider the potential impact of the Star Alliance on the application filed in this docket.

### **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 to the Alliance Expansion Agreement between United Air Lines, Inc. and Air Canada, subject to the proposed limits and conditions as set forth in (a), (b), and (c) below:

- (a) The approval and immunity granted in this proceeding shall not apply to operations involving all-cargo services or to operations involving services to or from third countries;

(b) The Joint Applicants shall not operate, use, or hold out service under a common name or brands without obtaining prior approval from the Department; and

(c) The approval and immunity granted in this proceeding is further subject to the terms, limitations, and conditions set forth in Appendix A hereto.

2. We tentatively direct United Air Lines, Inc. and Air Canada to resubmit their Alliance Expansion Agreement five years from the date of issuance of the final order in this case;
3. We tentatively direct Air Canada 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 its alliance partner United Air Lines, Inc.);
4. We tentatively direct United Air Lines, Inc. and Air Canada to submit any subsequent and/or subsidiary agreement(s) implementing the Alliance Expansion Agreement for review as described in footnote 40 *supra*;
5. We direct United Air Lines, Inc. and Air Canada within seven days of service of this order to provide the following information on the proposed Star Alliance:

Copies of commercial agreements (in final form, or in draft if there is no final agreement) between and among all of the six participating carriers;<sup>79</sup> information on the role of the Star Alliance agreements in the proposed United/Air Canada alliance in terms of corporate strategy, marketing, yield and capacity management, and pricing; information on the content, scope, and timing of the Star Alliance and how the Star Alliance partners may be integrated into the corporate strategy, code-sharing, yield management, and pricing of the United/Air Canada alliance, if approved; a detailed explanation of the Star Alliance agreement(s) (either in final or in draft form if not final), including all documents analyzing the proposed commercial arrangement, its competitive impact, and the role that the other Star Alliance members would play in the proposed United/Air Canada alliance in terms of corporate strategy, marketing, yield management, capacity management, and pricing; and complete information on the extent to which the Star Alliance would affect operations between the U.S. and Canada by United or Air Canada with respect to passengers with an origin or destination in third countries;

6. We direct that the information and evidence required in ordering paragraph 5 shall be filed within seven business days of the date of this order;

---

<sup>79</sup> Do not resubmit agreements or other documents filed in Dockets OST-96-1116, OST-96-1411, or OST-96-1434. However, provide any amendments, revisions, or subsidiary agreements (in final form, or in draft if no final amendment, revision, or agreement exists) to such previously filed documents.

7. We direct interested persons wishing (a) to comment on our tentative findings and conclusions, (b) to file objections to the issuance of the order described in ordering paragraphs 1-4, and/or (c) to comment on the information and evidence submitted in response to ordering paragraph 5, to file an original and five copies in Docket OST-96-1434 and serve a statement of such objections or comments together with any supporting evidence the commenter wishes the Department to notice on all persons on the service list in that docket no later than 28 days from the service date of this order. Answers to objections shall be due no later than 7 business days after the last day for filing objections/comments;<sup>80</sup>

8. If timely and properly supported objections are filed, we will afford full consideration to the matters or issues 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

9. We shall serve this order on all persons on the service list in this docket.

By:

**CHARLES A. HUNNICUTT**  
Assistant Secretary for Aviation  
and International Affairs

(SEAL)

*An electronic version of this document will be made available on the World Wide Web at:  
<http://www.dot.gov/general/orders/aviation.html>*

---

<sup>80</sup> Service should be by hand delivery or telefax. The original filing should be on 8½" by 11" white paper using dark ink and be unbound without tabs, which will expedite use of our docket imaging system.

**CONDITIONS GOVERNING THE ANTITRUST IMMUNITY FOR THE  
ALLIANCE EXPANSION AGREEMENT BETWEEN UNITED AIR LINES, INC.,  
AND AIR CANADA**

**Grant of Immunity**

The Department grants immunity from the antitrust laws to United Air Lines, Inc. and Air Canada, and their affiliates, for the Alliance Expansion Agreement dated May 31, 1996, between United Air Lines, Inc. and Air Canada and for any agreement incorporated in or pursuant to the Alliance Expansion Agreement.

**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 local U.S.-point-of-sale passengers flying nonstop between Chicago-Toronto and San Francisco-Toronto, or 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, implementation, promotion, or sale by the parties (including but not limited to pricing, inventory or yield management coordination, or pooling of revenues) of the following with respect to local U.S.-point-of-sale passengers flying nonstop between Chicago-Toronto and/or San Francisco-Toronto: 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 services offered under its own code. For immunity to apply, however: (i) in the case of corporate fare products and group fare products, local U.S.-point-of-sale nonstop Chicago-Toronto and San Francisco-Toronto traffic shall constitute no more than 25% of a corporation's or group's anticipated travel (measured in flight segments) under its contract with United and Air Canada; and (ii) 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 pairs in addition to Chicago-Toronto and/or San Francisco-Toronto.

In addition, despite the foregoing limitations, antitrust immunity shall extend to the joint development, implementation, promotion or sale by the parties (including but not limited to pricing, inventory or yield management coordination, or pooling of revenues) of restricted fares with respect to local U.S.-point-of-sale passengers flying nonstop between San Francisco-Toronto.

**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, which 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 (i) 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 (ii) wholesalers for sale by such wholesalers as part of tour packages in which air travel is bundled with other travel products, which 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.

"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, which discounts may be stated either as percentage discounts from specified published fares or net prices.

"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.

"Restricted fares" means published fares that require either a Saturday night stay or a minimum advance purchase of at least seven days.

**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 Expansion Agreement 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-Toronto and San Francisco-Toronto 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-Toronto and San Francisco-Toronto routes; 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; joint cargo programs; coordination of frequent flyer programs; coordination of travel agency commission and override programs and policies; and coordination of terms and charges for ancillary passenger services.

**Review of limitations on immunity**

Within eighteen months from the date that this Order becomes final, or at any time 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-Toronto and/or San Francisco-Toronto city pairs; 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.