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

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Joint Application of)

AMERICAN AIRLINES, INC.)

and)

LINEA AEREA NACIONAL CHILE,)

S.A. (LAN CHILE))

under 49 U.S.C. §§ 41308 and 41309 for)

approval of and antitrust immunity)

for alliance agreement)

Docket OST-97-3285 - 56

**JOINT CONSOLIDATED ANSWER OF
AMERICAN AIRLINES, INC. AND
LAN CHILE, S.A. TO OBJECTIONS**

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Dated: June 1, 1999

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**JOINT CONSOLIDATED ANSWER OF
AMERICAN AIRLINES, INC. AND
LAN CHILE, S.A. TO OBJECTIONS**

American Airlines, Inc. and Lan Chile, S.A. (“the Joint Applicants”) jointly submit this consolidated answer to objections filed by United Air Lines, Inc., Delta Air Lines, Inc., Continental Airlines, Inc., and Aeromexico to the Department’s Order to Show Cause (Order 99-4-17, April 22, 1999).

In a comprehensive decision that responds fully to the Department’s statutory mandate under 49 U.S.C. sections 41308 and 41309, the Department concluded that it is in the public interest to approve and grant antitrust immunity to the **American/Lan Chile** alliance. The Department found that approval would enable the two carriers to “operate more efficiently, and provide enhanced service options to the U.S. traveling and shipping public,” and would “be consistent with [U.S.] policy of facilitating our international aviation policy toward more open-skies relationships, and of encouraging competition among emerging multinational airline networks.” Order 99-4-1 7, at 2. The Department also noted that its decision was “consistent with our earlier actions approving and granting antitrust immunity for other alliances.” Id.

In its final order approving and granting antitrust immunity to the Delta/Swissair/Sabena/Austrian alliance, the Department concluded that “[t]he commenting parties have not raised any new arguments that would compel our changing our ultimate conclusion.” Order 96-6-33, June 14, 1996, at 8. That conclusion applies with equal force in this case. The objections fail to raise a single issue that might give the Department pause before proceeding to finalize the Order to Show Cause. In fact, the bulk of those objections simply rehash arguments previously raised by the same parties. The Department, in its Order to Show Cause, categorically addressed those arguments and concluded that they provide no basis for refusing to approve and immunize the American/Lan Chile alliance.

The Joint Applicants submit the following in answer to the objections raised:

1. As they have done in prior pleadings, United, Delta, and Continental each takes the extraordinary and self-serving position of asking the Department to reject the American/Lan Chile alliance in order to facilitate each of them in obtaining an alliance of their own with Lan Chile.’ As Lan Chile has previously explained, prior to entering into an alliance with American, Lan Chile held discussions with each of United, Delta, and Continental. Lan Chile concluded that an alliance with American is the best fit, and will provide the greatest benefits to its passengers. Now, these purportedly free market-oriented companies propose government

¹ See Objection of Delta Air Lines, Inc., May 20, 1999, at 12 (“an alliance between Delta and Lan Chile would inject a strong new entrant”); Statement of Objections of United Air Lines, Inc., May 20, 1999, at 16 (“by entering into an alliance, United and Lan Chile could improve the efficiency of their Miami-Chile services”); Objections of Continental Airlines, Inc., May 20, 1999, at 11 (“a Lan Chile alliance with Continental or another carrier would expand options”).

intervention as a means of achieving a goal (i.e., an alliance with Lan Chile) that each has failed to attain in the marketplace.²

2. United, Delta, and Continental would prefer to jettison the obvious benefits of U.S.-Chile open skies rather than embrace the competitive challenges and opportunities that open skies offer. In October 1997, when the United States and Chile initialed an open skies agreement, Chile made clear that it would sign the agreement only after satisfactory regulatory approvals and immunity were granted to the Lan Chile/American alliance. That position has been consistent throughout this proceeding.

United, Delta, and Continental must face the reality that the only two options available are open skies with approval of the American&an Chile alliance -- which promises unrestricted new competitive opportunities for all U.S. and Chilean carriers -- or the restrictive status quo, which promises no new opportunities at all.³ The bottom line remains that, while the status quo restricts new entry, there is a strong likelihood of new entry and a wider range of service options under open skies.⁴

² Delta's position is particularly inconsistent. On the one hand, Delta urges the Department to intervene and prevent the **American/Lan Chile** alliance. On the other, Delta urges a "hands off" approach and argues that the Department's policy of "attempting to redraft commercial agreements to eliminate exclusivity clauses" is "[p]lacing limits on carriers' freedom of contract choices." Objection of Delta Air Lines, at 12-14. See also Petition for Reconsideration of Delta Air Lines, Inc., May 25, 1999 (Docket OST-99-5726) (attacking the Department's disapproval of exclusivity clauses).

³ United, Delta, and Continental surely do not favor the status quo. United, for example, complains that it, along with Delta and Continental, is "effectively frozen out of the U.S.-Chile market today by the restrictive terms of the current bilateral agreement." Objections of United Air Lines, at 8. However, open skies will eliminate those very restrictions.

⁴ On October 30, 1997, Delta issued a press release stating that the initialed U.S.-Chile open skies agreement "is a welcome boost to Delta's plans . . . to provide service throughout the hemisphere." On April 22, 1997, Delta applied to serve Santiago from Atlanta (Docket OST-97-(continued..))

3. United, Continental, Delta, and Aeromexico (Delta's "strategic marketing" partner⁵) argue that, notwithstanding the prospect of implementation of the U.S.-Chile open skies agreement, the Department's approval of and grant of antitrust immunity to the **American/Lan Chile** alliance would be fatal to competition, not just in the U.S.-Chile market, but variously in the Southern Cone, South America, and Latin America generally.

The potential effects of the Lan Chile/American alliance have been the subject of months of exhaustive scrutiny by the Department of Justice Antitrust Division and the Department of Transportation. If the Justice Department (which is a far more objective and reliable source than the objecting airlines) had determined that the Department's tentative approval of the Lan Chile/American alliance were flawed and failed properly to consider the competitive issues, the Justice Department would have filed an objection of its own. The Justice Department has a demonstrated policy of stating publicly its concerns about particular alliances, as reflected in its comments on the Department's show-cause orders in both the **Delta/Swissair/Sabena/Austrian** and **American/TACA** proceedings. Significantly, however, the Justice Department has not submitted comments on the Order to Show Cause in this case.⁶

(. . . continued)

2372), and on December 10, 1997, applied to serve Santiago from New York (JFK). (Docket OST-97-32 18). Continental presently serves Santiago from Newark, and under open skies is likely to add nonstop service from its hub at Houston. Late last year, Continental ordered 10 Boeing wide-body jets, reportedly for use on new trans-Atlantic and Latin American routes. See Wall Street Journal, November 20, 1998.

⁵ "Delta and Aeromexico Plan Expanded Relationship, Including A Five-Year Marketing Agreement," Delta Air Lines Press Release, March 10, 1998.

⁶ Delta quotes from the Justice Department's comments in the **American/TACA** proceeding in support of its claim that the **American/Lan Chile** alliance is anti-competitive. Objection of Delta Air Lines, at 9. However, the Justice Department's silence in this case provides the most eloquent testimony to the inapplicability of its comments on the **American/TACA** matter here.

4. United and Delta restate their assertions that the American/Lan Chile alliance will not generate benefits similar to those allegedly created by the antitrust-immunized trans-Atlantic alliances. They argue that Santiago lacks sufficient connecting traffic to warrant designation as a South American hub, which, they contend, differentiates Santiago from the European hubs of United's, Delta's, and Northwest's trans-Atlantic alliance partners. Therefore, they conclude, the American&an Chile alliance cannot offer the sort of positive "network effects" allegedly achieved in the trans-Atlantic market.

Santiago may be a regional hub and not a mega-hub like Frankfurt, but that should not disqualify Chilean carriers from participating in the developing global alliance trend, and it provides no basis for refusing to approve and grant immunity to the American/Ian Chile alliance.' The Department's Order to Show Cause directly rebuts United's and Delta's argument:

[N]etwork effects are an important reason why we expect an open-skies agreement with Chile to result in more intense competition than now exists. Chile will become an important spoke that will feed traffic through competing global networks. This is precisely the type of market envisioned and promoted by the U.S.-Chile open-skies accord and by our overall international aviation policy.

Order 99-4-17, at 18.

Revisiting a related theme, United, Delta, and Continental suggest that the Department's approval of the American/Lan Chile alliance will preclude them from developing competing alliances in the South American region. Quite apart from the absence of any basis for these overblown predictions, the carriers neglect to mention that they already have established

⁷ The fact that neither Vienna nor Stockholm is a mega-hub did not disqualify the Delta/Swissair/Sabena/Austrian and United/Lufthansa/SAS alliances respectively.

significant alliance networks -- both regional and global. United fails to reference its well-established alliance with VARIG, South America's largest carrier, as well as its global Star Alliance with such major international carriers as Lufthansa, SAS, and Air Canada. Delta, meanwhile, omits reference to its Latin American regional partners Aeromexico, and Transbrasil, as well as its Atlantic Excellence Alliance with Swissair, Sabena, and Austrian Airlines.

Finally, Continental is allied regionally with ACES, VASP, Aserca, and most recently, COPA,⁸ in addition to its U.S. partnership with Northwest Airlines and its international partnerships with Air France and Virgin Atlantic Airways, among others. In fact, just four days after objecting that American is "pre-empting more competitive alliances" in Latin America,' Continental acclaimed its new partnership with COPA as "one of the most important strategic alliances in Latin American aviation.,'⁰

Under open skies, United, Delta, and Continental and their partners will have the flexibility to offer competitive code-share service in the U.S.-Chile market, to operate their own direct services, or both. In addition, each international alliance network will be able to feed traffic to and from Chile and other points in Latin America to Europe, Asia, and elsewhere. This

⁸ "Copa Airlines Takes Off With New Aircraft, Image; Airline Initiates Code-share With Alliance Partner Continental Airlines," Continental Airlines Press Release, May 24, 1999 (announcing the June 10, 1999 commencement of code-sharing between Continental and COPA "throughout Latin America"). Like American with Aerolineas Argentinas, Continental has made an equity investment in both COPA and ACES. However, unlike American/Aerolineas, Continental already has commenced implementation of its alliances with COPA and ACES. Continental also reportedly is planning to acquire a stake in Aeroperu. "Peru Optimistic Continental Will Reach Deal On Aeroperu," Dow Jones, May 26, 1999.

⁹ Objections of Continental Airlines, at 4.

¹⁰ "Copa Airlines Takes Off With New Aircraft, Image; Airline Initiates Code-share With Alliance Partner Continental Airlines," Continental Airlines Press Release, May 24, 1999.

is precisely the kind of global network competition that the Department had in mind when it cited the positive network effects of alliance approval and implementation of open skies. In fact, in terms of global network competition, United and Delta, with their respective trans-Atlantic alliances having been operating with antitrust immunity for the past three years, enjoy a considerable competitive advantage over American, whose proposed alliance with British Airways continues to await implementation.

5. Continental, Delta, and Aeromexico take the position that the Department should disapprove the American&n Chile alliance in order to prevent American from “manipulat[ing] open skies in Chile and closed skies in Argentina” through a purported tripartite linkage between American, Lan Chile, and Aerolineas Argentinas that will allegedly control traffic between the United States and the Southern Cone and within Latin America.¹² There is no such linkage. Lan Chile’s code-share alliance with American is bilateral; it does not involve Aerolineas Argentinas or any other carrier. For its part, Lan Chile resents the implication that it is no more than a pawn in American’s alleged regional strategy.

Continental’s and Delta’s attempt to interpose a new trilateral U.S.-Chile-Argentina dimension into this proceeding and to tie this proceeding to the progress of U.S.-Argentina

¹¹ Objections of Continental Airlines, at 3.

¹² Objections of Continental Airlines, at 3-4; Objection of Delta Air Lines, at 3; Reply of Aerovias De Mexico, S.A. de C.V., May 20, 1999, at 2-3.

bilateral talks is unfounded and extreme.¹³ In fact, if this proceeding and the prospect of U.S.-Chile open skies have any impact on Argentina, it may be in exerting pro-competitive pressure on Argentina to follow Chile's lead and sign an open skies agreement. Arguably, the U.S.-Chile open skies agreement already has lent momentum to the U.S.-Argentina talks, which, notwithstanding the recent postponement, have encompassed three rounds of negotiations since last December -- demonstrating a persistent bilateral commitment to open skies. In any event, the Joint Applicants' understanding is that Argentina has a good faith interest in entering into an open skies agreement, but that the principal unresolved issue is the duration of any transition to open skies.¹⁴

6. United asserts that it "has been seeking to develop a network of services at Miami," and argues that approval of the **American/Lan Chile** alliance will erode such efforts. Objections of United Air Lines, at 15. For its part, American responds that United's position in the Miami market is due to United's own decisions, over a period of more than seven years, not to invest in building a Miami hub. When United acquired Pan Am's Latin American route

¹³ Continental recently asked the Department to postpone further action in this proceeding indefinitely, or at least until 60 days after a new U.S.-Argentina agreement is reached. Motion of Continental Airlines, Inc. for Extension of Time, May 3, 1999. Lan Chile identified the dangers inherent in that request. Answer of Lan Chile, S.A. to Motion of Continental Airlines, Inc., May 12, 1999. The only apparent objective behind Continental's motion is to delay approval of the American&n Chile alliance and implementation of U.S.-Chile open skies for as long as possible.

¹⁴ Continental and Delta imply that American has a vested interest in maintaining the U.S.-Argentina status quo by obstructing progress toward open skies. See Objection of Delta Air Lines, at 3 ("[t]he U.S.-Argentina talks were torpedoed"); Objections of Continental Airlines, at 3 n.3 ("Argentina postponed aviation talks with the U.S. indefinitely"). In fact, Continental is incorrect: Argentina has requested that talks resume in August. More importantly, Continental's and Delta's implication is ludicrous: if anything, open skies would likely be an essential pre-condition to any expansion of the **American/Aerolineas** relationship into code-share operations.

system in 1992, United was well-positioned to match American at Miami, but chose to devote its resources elsewhere, particularly in Asia, where United enjoyed the protection of a highly restrictive U.S.-Japan bilateral agreement. United withdrew most of its Miami-Central American services in 1994, long before the *American/TACA* alliance was announced, and more recently chose to transfer Miami-Sao Paulo and Miami-Buenos Aires services to Chicago. Because of United's lack of commitment to Miami, United would be a poor alliance partner for Lan Chile, which requires a strong Miami presence to strengthen its network and maximize benefits for its Chile-U.S. passengers, as well as to compete in the U.S.-South America market with *United/VARIG*, *Delta/Aeromexico*, *Delta/Transbrasil*, *Continental/COPA*, and other regional alliances.

7. Continental objects that certain conditions proposed by the Department are less restrictive than those imposed on the *American/TACA* code-sharing arrangement. Continental claims that “[t]he *American/Lan Chile* alliance is immunized for three years, which is one year more than the *American/TACA* alliance.” Objections of Continental Airlines, at 13. Continental seems to be unaware that the *American/TACA* case did not involve a request for antitrust immunity! In fact, the Department's proposal of a three-year term in this case is significantly less than the five-year period used for the antitrust-immunized alliances of *Northwest/KLM* (Order 93-1-11, January 11, 1993); *United/Lufthansa* (Order 96-5-27, May 20, 1996); *Delta/Swissair/Sabena/Austrian* (Order 96-6-33, June 14, 1996); *American/Canadian* (Order 96-7-21, July 15, 1996); and *United/Lufthansa/SAS* (Order 96-11-1, November 1, 1996).¹⁵

¹⁵ Continental also misconstrues the Department's Show Cause Order by insisting that “the Department should require an eighteen-month review of the conditions on the *American/Lan Chile* alliance to ensure additional conditions are placed on the alliance if indicated by (continued. . .)

Continental also objects that the Department has not prohibited American and Lan Chile from forming “a joint alliance committee and engaging in any preferred information sharing activities on current or prospective fares or seat availability between the U.S. and South America.” Objections of Continental Airlines, at 14. Once again, Continental draws a misplaced comparison to the non-immunized **American/TACA** code-sharing partnership. Continental fails to appreciate that such activities provide the basis of the Joint Applicants’ request for antitrust immunity and are entirely consistent with the immunized practices of the **Delta/Swissair/Sabena/Austrian**, **United/Lufthansa&AS**, and **Northwest/KLM** alliances.

Finally, Aeromexico proposes that the Department broaden the proposed immunity limitation (carve-out) condition to include the New York-Santiago and Miami-Chile markets. These are one-stop and connecting markets for Lan Chile and American. The Department has never applied a carve-out condition to other than nonstop markets, and Aeromexico offers no reason for the Department to do so here. Aeromexico provides no data of any sort to support or justify such a condition. In terms of the New York-Santiago market, Aeromexico further fails to acknowledge that Continental’s inauguration of Newark-Santiago service added a major (and the only nonstop) competitive alternative. Aeromexico also ignores the wide range of competitive one-stop connecting services available. By contrast, the Department has carefully reviewed the relevant traffic data and concluded that the only market warranting a limited carve-out is **Miami-Santiago**.

(. . . continued)

competitive conditions.” Objections of Continental Airlines, at 14. However, the Department did propose just such a condition. See Order 99-4-1 7, App. A, at 3.

8. United criticizes the Department for its finding that the Miami-Santiago market “accounts for only a relatively small share of total U.S.-Chile demand.” Specifically, United states that it “is persuaded that the 15% figure cited in the Order is erroneous.” Objections of United Air Lines, at 4, Order 99-4-17, at 18 n.29. It states that “Miami-Santiago local passengers represent between 40% and 50% of total U.S.-Chile demand.” Objections of United Air Lines, at 4.

United apparently misconstrues the Department’s application of the O&D survey data. The Department found that “[o]nly 15 percent of the total U.S.-Chile passenger traffic were to/from American’s Miami gateway” (i.e., 15 percent of the traffic flown was on American). Order 99-4-17, at 18 n.29. As to United’s “between 40% and 50%” pronouncement, this estimate crosses the threshold between the tolerably vague and the irresponsibly speculative. It also is incorrect. American on numerous occasions has reviewed the relevant traffic data, which show that Miami-Santiago local passengers comprise approximately 21 percent of the total U.S.-Chile market.¹⁶ In any event, United’s point is essentially moot, as the Department already has proposed to apply an immunity “carve out” limitation to the Miami-Santiago market, which should address whatever concern United was seeking to articulate.

9. United and Continental argue (and speculate) that recent trends in the Miami-Central America market following the Department’s approval of the **American/TACA code-share partnership** are a harbinger of anti-competitive effects of an **American/Lan Chile alliance**. Such arguments provide no grounds for the Department to reverse its position in this case.

¹⁶ 1998 Annual DOT U.S. carrier O&D Survey data. Miami-Santiago is the only overlap nonstop city-pair market involved in the Lan Chile/American alliance.

In the first place, U.S.-Central American markets are different from the U.S.-Chile market. Second, the carriers rely on the wrong facts. United claims that total flights between Miami and nine principal Central American destinations are due to decline by 10 percent for the year ending July 1999.” In fact, a review of traffic data for the more relevant U.S.-Central America market reveals that, while total flights have declined by a statistically insignificant three percent,* frequencies to Central America from U.S. gateways other than Miami have increased dramatically. Specifically, frequencies from Atlanta have risen by 25 percent, Dallas/Ft. Worth by 50 percent, Newark by 20 percent, New York (JFK) by 63 percent, and New Orleans by 41 percent.¹⁹ In sum, contrary to United’s dire warnings, competition in the U.S.-Central America market appears alive and well.

Thus, close scrutiny of traffic data for the U.S.-Central America market offers no credible evidence that competition in that market has declined over the past year. Moreover, even if the data did support United’s assertions, United fails to establish that there is any meaningful correlation between trends in the U.S.-Central America market and the prospects for the U.S.-Chile market following the implementation of U.S.-Chile open skies.

¹⁷ Objections of United Air Lines, at 5. United states that it analyzed flights between Miami and nine principal destinations in Central America, but fails to identify those city-pairs. American reviewed traffic between Miami and eight principal Central American destinations: San Jose, Guatemala City, Panama City, San Salvador, Belize, Managua, San Pedro Sula, and Tegucigalpa. That review indicates that Miami-Central America traffic is down by eight percent. American and COPA have not reduced their frequencies at all, while Iberia has increased its MIA-GUA service by no less than 39 percent. The decline is largely attributable to Nica’s reduction of MIA-MGA service from twice to once daily and TACA’s suspension of its MIA-BZE service.

¹⁸ The relatively marginal overall decline in frequencies may be attributed to United’s withdrawal of service at ORD and IAD.

¹⁹ OAG, July 1998/July 1999.

* * *

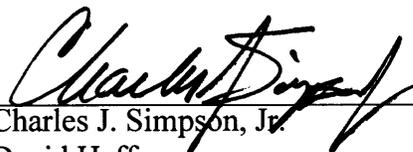
In conclusion, the objections of United, Delta, Continental, and Aeromexico do little more than revisit old arguments that the Department thoroughly addressed in its Order to Show Cause. The objections also fail to raise any new issues that would justify the Department's alteration of any of the findings and conclusions contained in that Order.

WHEREFORE, American and Lan Chile respectfully urge the Department to issue a Final Order finalizing the tentative findings in the Order to Show Cause as soon as possible.²⁰

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Dated: June 1, 1999

²⁰ The final order should also approve the American/Lan Chile code-sharing applications submitted on October 7, 1997 (OST-97-2982 and undocketed), which were consolidated into this proceeding by Order 98-2-21, February 20, 1998, but which were not fully addressed in the ordering paragraphs of the Order to Show Cause.

CERTIFICATE OF SERVICE

I hereby certify that on this 1st day of June, 1999, a copy of the foregoing Joint Answer of American Airlines, Inc. and Lan Chile, S.A. was served by first class mail, postage prepaid, on the parties named below:

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