

# ORIGINAL

BEFORE THE  
DEPARTMENT OF TRANSPORTATION  
OFFICE OF THE SECRETARY

DEPARTMENT OF TRANSPORTATION  
OFFICE OF THE SECRETARY  
August 11, 1999

61928

Joint Application of )  
 )  
ALITALIA-LINEE AEREE ITALIANE- )  
S.p.A. )  
and )  
KLM ROYAL DUTCH AIRLINES )  
and )  
NORTHWEST AIRLINES, INC. )  
 )  
for approval of and antitrust )  
immunity for agreements pursuant )  
to 49 U.S.C. §§ 41308 and 41309 )  
 )

Docket OST-99-5674 - 27

ANSWER OF THE INTERNATIONAL ASSOCIATION  
OF MACHINISTS AND AEROSPACE WORKERS, AFL-CIO  
TO THE JOINT APPLICATION

The International Association of Machinists and Aerospace Workers, AFL-CIO ("IAM") hereby opposes the joint application of Alitalia-Linee Aeree Italiane-S.p.A. ("Alitalia), KLM Royal Dutch Airlines ("KLM") and Northwest Airlines ("Northwest") (collectively the "joint applicants") for approval of and anti-trust immunity for alliance agreements pursuant to 49 U.S.C. §§ 41308 and 41309.<sup>1</sup> As demonstrated below, the application should be denied in its entirety for the following reasons:

- (1) as a result of the current relationships between Northwest and Continental, Alitalia and Continental, and KLM and Alitalia, which the joint applicants do not

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<sup>1</sup> On August 6, the Department granted the IAM's motion for an extension of time to file an answer in this case until August 23, 1999. Joint Application, OST-99-5674, Order 99-8-5.

address, the proposed alliance will substantially reduce competition and is not in the public interest; and

(2) the application is not in the public interest based upon **Alitalia's** abysmal labor relations record, its most recent demonstration of bad faith bargaining with the **IAM**, and the fact that, if the alliance is approved, the **IAM** intends to extend its picket line against Alitalia to Northwest and KLM.

I. **BASED UPON THE RELATIONSHIPS WHICH CURRENTLY EXIST BETWEEN NORTHWEST AND CONTINENTAL, CONTINENTAL AND ALITALIA, AND KLM AND ALITALIA, THE PROPOSED ALLIANCE WOULD SUBSTANTIALLY REDUCE COMPETITION AND IS NOT IN THE PUBLIC INTEREST.**

In reviewing an application which seeks approval of and antitrust immunity for an alliance, the Department must determine the effects the proposed alliance will have on competition and the public interest. Under 49 U.S.C. § 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.

**Joint Application of American and Lan Chile**, OST-97-3285-47, Order 99-4-17, at 14.

Under 49 U.S.C. § 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. The Department may not approve an inter-carrier 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.

Joint Application of American and Lan Chile, OST-97-3285, Order 99-4-17, at 14.

In applying this standard and in assessing the effects of an application upon competition and the public interest, the Department must be provided with all the facts relevant to the proposed alliance as well as the relationships which currently exist between the joint applicants and other airlines. In the instant Application, the parties have omitted and mischaracterized facts essential to the DOT's analysis. Currently, the joint applicants enjoy alliances either with each other or with Continental which substantially affect the impact the proposed venture will have upon competition and the public interest. Rather than provide a fully developed picture of the interactions between each of these carriers, the joint applicants have provided a substantially cropped snapshot in which Continental does not even appear. In order for the Department properly to consider this application, it must take into account the existing relationships between Northwest and Continental, Alitalia and Continental, and KLM and Alitalia. In addition, as a result of misrepresentation and omission of the current partnerships between the applicants and Continental, the parties have submitted responses to the DOT's information requests which, concomitantly, are inaccurate **and** incomplete.

**A. Northwest and Continental.**

On November 20, 1998, Northwest completed the acquisition of 8.7 million **shares** of Continental stock, which were deposited in a voting trust. Six weeks later, in January 1998, Northwest and Continental began the coordination of their schedules and an extensive code-sharing relationship. According to the Department of Justice, in an amended complaint filed on December 18, 1998, the acquisition of equity and other related transactions resulted in Northwest acquiring voting control of Continental. That control, the DOJ alleges, will **"substantially lessen competition"** in violation of the Clayton Act, 15 U.S.C. §§ 18 and 25, and **"unreasonably restrain trade"** in violation of the Sherman Act, 15 U.S.C. §§ 1 and 4, in the following ways:

1. Actual and potential competition between Northwest **and** Continental for nonstop scheduled airline passenger service in the hub-to-hub markets will be reduced or eliminated:
2. Actual and potential competition between Northwest and Continental for scheduled airline passenger service in city-pair markets where Northwest and Continental are dominant providers of connecting service will be reduced or eliminated:
3. Competition generally in numerous city-pair markets for scheduled airline passenger service may be lessened substantially;
4. Coordinated pricing activity between providers of scheduled airline passenger service likely will be facilitated: and
5. Prices for scheduled airline passenger service in numerous concentrated city-pair markets in the United States are likely to increase.

Amended Complaint, United States v. Northwest and Continental Airlines, Civil Action No. 98-74611, at 14 (Exhibit 1).

The Justice Department's Complaint confirms what the General Accounting Office concluded in January 1996, in its report on the competitive effects of the various domestic airline alliances including Northwest and Continental. The GAO concluded that,

It is difficult to determine precisely how the [Northwest and Continental] alliance will affect competition, but the industry experts' concerns and the airlines' past records establish cause for concern. As discussed, there is widespread agreement among these experts that competition will likely decline over time as firms recognize their interdependence and maintain prices above the competitive level.

United States General Accounting Office, Report to Congressional Requesters, Aviation Competition, Effects on Consumers from Domestic Airline Alliances Vary, January 1999, at 22.<sup>2</sup>

Thus, both the GAO and the DOJ agree that the Northwest and Continental relationship, whether it is the product of control or mere coordination, will severely undermine competition and thereby harm consumers.

But the Northwest-Continental relationship is nowhere mentioned in the Northwest-Alitalia application. By not addressing or even referring to the extensive integration of Northwest's and Continental's operations, the joint applicants have described **an** alliance which is fundamentally at odds with reality. The parties would have the Department believe that Continental is as much a competitor of Northwest as is any other major carrier. The truth,

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<sup>2</sup> It should be noted that when GAO reached this conclusion, it relied upon the claim of Northwest and Continental that they would not implement code-sharing on the seven hub-to-hub routes they both serve. Currently, Northwest and Continental, in **fact code share** on at least some of these routes including **Newark-Minneapolis** and **Houston-Memphis**.

which the joint applicants so blithely ignore, is that through the Northwest and Continental relationship, these two carriers now control 20% of the traffic flown by major carriers. Aviation Daily, August 19 at 8. Even if the joint applicants were just to concede that Continental is something less than a traditional rival of Northwest, it would be incumbent upon them to explain how Continental's status enhances the competitive power of the proposed alliance.

**B. Alitalia and Continental.**

Northwest's control of, and coordination of schedules with, Continental is further implicated in the joint application by the fact that Continental and Alitalia currently enjoy a code-sharing relationship. As approved by the Department, Alitalia may place its designator code on Continental flights between Newark and Detroit, Cleveland, San Francisco, Houston, Philadelphia, Washington D.C. and Atlanta. In addition, Continental and Alitalia code-share on flights between Newark and Rome. Joint Application of Alitalia and Continental, OST-95-347, 348, Order 96-U-15; OST-97-2113, Order 97-3-27. The parties, however, refuse to address this service, even though the Department has specifically asked them to provide "an analysis of the competitive effect in city-pair markets where Continental competes, or engages or may engage in cooperative arrangements with **Alitalia**". Joint Application, OST-99-5674, Notice Requiring Supplemental Information, dated June 22, 1999. The application contains no such

analysis and in fact, does not even refer to the relevant **city-** pairs operated by Continental and Alitalia.

Whether as a controlling partner of Continental or merely as a beneficiary of an extensive code-sharing relationship, Northwest has every reason to ensure that Continental does not unnecessarily dilute its market share on **any** route to Europe and more specifically, to Italy. Clearly, if the alliance is approved, Northwest will coordinate its schedule with Continental on its transatlantic service to the same extent as it now coordinates with Continental on domestic routes.

In fact, that kind of coordination may very well exist today. Notwithstanding the applicants' repeated assertion that Northwest **"does** not serve Italy, either directly or on a codeshare **basis"** the carrier offers service from Minneapolis to Rome through Amsterdam on KLM. Joint Response to Order 99-5-10 at 4; see also Application at 14, 21. While the service may be operated by **KLM**, tickets on Flights 664 (Minneapolis-Amsterdam) and 1596 (Amsterdam-Rome) carry Northwest% designator code.

Continental also currently serves the Minneapolis-Rome market on a code-share basis. For example, Continental% code appears on Flight 315 (Minneapolis to Newark) and Flight 601 (Newark to Rome). The domestic portion is flown by Continental, whereas the transatlantic leg is operated by Alitalia. Clearly both Northwest and Continental provide service from Minneapolis to Rome. Nonetheless the joint applicants claim that Northwest **"does** not compete with Continental in any U.S. -Italy city-pair market." This

statement is only true if the alliance between the two carriers, which the joint applicants ignore, is considered. As partners, Northwest and Continental, on this route as with all others, do not compete but rather coordinate their schedules.

In fact, the cooperation that currently exists is not limited to the coordination of schedules but extends to a full integration of service among the joint applicants and Continental. Today, on flights from Minneapolis to Rome which are listed as Continental, Northwest operates the domestic leg, with one **exception**.<sup>3</sup> Of the joint applicants Northwest and **KLM** are not the only parties currently aiding each other and/or Continental in its service from Minneapolis to Rome. On a Minneapolis to Rome flight for which Northwest is the listed carrier, **KLM** operates the **Minneapolis-Amsterdam** segment and Alitalia operates the flight from Amsterdam to **Rome**.<sup>4</sup>

By omitting any discussion of the Northwest and Continental partnership, the joint applicants evade answering yet another inquiry by the Department. In its Notice Requiring Supplemental Information, the DOT requests a "description of whether and if so how Continental's operations will be integrated with those of the proposed alliance." The parties acknowledge that Continental will

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<sup>3</sup> For example, on October 10, 1999, Continental's schedule for Minneapolis to Rome lists, for the Minneapolis-Newark segment, Flights 5766, 5772, 5100, 5770 and 5306. Each flight is, in fact, operated by Northwest.

<sup>4</sup> In its schedule for October 10, 1999, Northwest is the listed carrier for Flight 664 (Minneapolis-Amsterdam) and Flight 4531 (Amsterdam-Rome). The first flight is operated by KLM and the second by Alitalia.

be included in the alliance, yet they refuse to provide a response to the second half of the question - how will Continental's be integrated with those of the proposed alliance. Rather than answer, the joint applicants declare that at this time the issue of integration remains a mystery and once resolved, they will submit an application to the Department. Again, the parties have embraced a strategy of concealing rather than dealing with the truth. As shown above, Northwest and Continental have already coordinated their flight activity and Continental currently integrates at least a portion of its operations with Alitalia. Based upon the existing cooperation between the parties and Continental, its membership in the alliance is already a fait accompli. Accordingly, a critical issue that must be resolved is to what extent Continental is and will be integrated into the alliance. If the parties insist that they cannot answer that question today, the Department should defer consideration of the application until they can do so.

**C. KLM and Alitalia.**

The joint applicants obliquely refer to the partnership which currently exists between KLM and Alitalia. Their description of the effects of the alliance upon their relationship is limited to the following statement, "**In** the expanded alliance, Alitalia and KLM will cooperate in developing these [U.S.-Italy] services via **Amsterdam.**" Joint Response to Order 99-5-10, at 5. Absent from the application, is any acknowledgment that such cooperation is occurring today and will intensify substantially in the future. The parties do not disclose that KLM and Alitalia have signed,

"... a joint-venture agreement to fully integrate their global operations under a single management, paving the way for an eventual merger of the two flagship carriers. The agreement, . . . set to take effect Nov. 1, will effectively merge the passenger and cargo operations of the Italian and Dutch carriers and create a fleet with one of Europe's largest capacities. It would be the most profound alliance between two independent airlines and would open the door to further integration. **KLM** already has a joint venture with Northwest Airlines of the U.S. for flights across the North Atlantic and certain other routes, and the two airlines say they aim to integrate Alitalia into that alliance shortly. The trio then plan to bring Continental Airlines of the U.S. in to create a four-way venture."

Wall Street Journal, August 2, 1999, at A12.

The joint applicants do not discuss or even refer to this agreement and its impact upon competition and the public interest. Without this information, the Department cannot properly assess whether the application satisfies the statutory standards. On this basis alone, the application should be denied.

In sum, if the Department is to determine the competitive effects of an application and its impact upon the public interest, it must be provided with an accurate and complete description of the parties' operations and the relationships which may already exist among them and with other airlines. Here, the application submitted is complete only in its distortion of the proposed alliance. The parties have provided virtually no information regarding the relationships between Northwest and Continental, and **KLM** and Alitalia. In discussing the Alitalia-Continental partnership, the applicants conveniently ignore the fact that these two airlines currently offer service in the same city-pair markets as do Northwest and **KLM**.

Apparently, the applicants assume that the Department will treat their application in a vacuum, as if none of the participants have either current or contemplated relationships with another airline. Thus, according to the applicants, the fact **that** Northwest controls or, at a minimum, coordinates with Continental is of no consequence to the DOT's consideration of their application. Rather than grapple with the intertwined network of operations which exists among them and other carriers, the applicants would prefer to present a far less complicated, though unrealistic, picture of their proposed alliance and its effects. Their efforts must be rejected. Accordingly, the Department should deny the application, or at a minimum, defer consideration until such time as the joint applicants respond in full to each of the questions they have yet to answer.

**II. THE APPLICATION IS NOT IN THE PUBLIC INTEREST BASED UPON ALITALIA'S ABYSMAL LABOR RELATIONS RECORD, ITS MOST RECENT DEMONSTRATION OF BAD FAITH BARGAINING WITH THE IAM AND THE FACT THAT, IF THE ALLIANCE IS APPROVED, THE IAM INTENDS TO EXTEND ITS PICKET LINE AGAINST ALITALIA TO NORTHWEST AND KLM.**

As evidenced by the Department's inquiry concerning the status of negotiations between Alitalia and the IAM, it is clear that the DOT's assessment of the impact the proposed alliance will have on the public interest must include the applicants' labor relations record. Joint Application, Order 99-5-10, at 2. Indeed, one of the enumerated considerations which define the public interest is "encouraging fair wages and working conditions." 49 U.S.C. § 40101. As shown below, Alitalia has demonstrated no genuine interest in resolving a dispute they began almost six years ago by

locking out **IAM-represented** employees. By granting the application, the DOT would be effectively endorsing **Alitalia's** conduct.

As the Department is aware, the **IAM** recently met with representatives of Alitalia to resolve a dispute which commenced in September 1993 when Alitalia locked out 150 **IAM-represented** employees. That dispute grew out of negotiations for a collective bargaining agreement covering **Alitalia's** employees in its cargo, traffic (passenger service) and reservations departments. The **IAM** has represented Alitalia employees for forty-seven years. Negotiations to amend the then current collective bargaining agreement began in 1990. Three years later, the parties had exhausted the bargaining procedures under the Railway Labor Act and were free to engage in self-help, meaning the **IAM** could strike the carrier and Alitalia could unilaterally impose changes to the collective bargaining agreement. Declaration of Joseph Adinolfi ("**Adinolfi Decl.**"), at ¶¶ 1-4 (Exhibit 2).

On the last day of negotiations before the self-help period was to begin, Alitalia made what it termed "**its last best offer.**" Although the **IAM** negotiating committee did not endorse this proposal, in accordance with **IAM** policy they intended to present it to the membership for a ratification vote. During that balloting the MM-represented employees of Alitalia would also be given the opportunity to vote to strike the airline in the event the company's offer were rejected. Before the **IAM** could hold these ratification meetings, Alitalia informed the employees who reported to work on both the midnight and day shifts on September 3 that

they were barred from entering the property and would not be permitted to work. Alitalia thereby initiated a lock-out of the **IAM membership**.<sup>5</sup> In response, the membership rejected the agreement and voted to strike against the airline. Adinolfi Decl., at ¶¶ 5-10.

The joint applicants blatantly misstate the facts when they assert that Alitalia did not engage in a lock-out. Joint Response to Order 9-5-10, at 8. There is no doubt that security guards hired by Alitalia barred **IAM-represented** employees from working on September 3, 1993. As with the rest of the application, the parties would prefer to misrepresent their record rather than confront the issues the truth presents.

Since September 3, 1993, Alitalia has continued its lock-out and has evidenced, at best, a sporadic interest in resuming negotiations. In May 1999, shortly after the filing of the Application at issue, Northwest offered to assist the parties in resolving their dispute and in reaching a collective bargaining agreement. As a result of Northwest's intervention, negotiations were scheduled for July 6, 1999. At that meeting, the **IAM** made a proposal to settle all outstanding issues. In response, **Alitalia's** representative informed the **IAM** that they would need an extended period of time to study the proposal. The parties agreed to schedule the next negotiations session for two days, August 5 and

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<sup>5</sup> Several days later, an Alitalia manager notified the **IAM** membership that there had not been a lock-out. When an **IAM** representative, however, sought confirmation of this notice, the same Alitalia manager informed him that the employees would not be allowed to return to work. Adinolfi Decl., at ¶ 9.

6, in order to give the parties ample time to reach an agreement. Adinolfi Decl., at ¶¶ 11-14.

On August 5, 1999, in its response to the **IAM's** proposal, Alitalia offered a severance package of \$1.9 million and an improved pension. While Alitalia specified the value of the severance each employee would receive, the carrier provided only a general statement regarding the improvement to an individual's pension benefits. When the **IAM** attempted to engage Alitalia in negotiations over the carrier's pension and severance proposals, **Alitalia's** representatives stated that they would not proceed with these negotiations until they had determined the amount of overfunding in the union pension plan. As a result negotiations ended on August 5 and were scheduled to resume on August 19. Adinolfi Decl., at ¶¶ 15-16.

The issue of possible over-funding was first raised by **IAM** representatives in 1997. At that time the **IAM** suggested that if the pension plan were over-funded, this could provide the carrier with another source of money to bridge the economic gap in the parties' proposals. It was not until the meeting on August 5, 1999 that the Company took the position that it could not negotiate until the amount of over-funding was determined. **Alitalia's** representative could not explain why this figure had not been calculated in the four weeks since the last meeting on July 6. Adinolfi Decl., at ¶ 14.

On August 17, Alitalia informed the **IAM** that the union pension plan was over-funded by \$2.7 million. At the August 19 meeting,

Alitalia stated that the total settlement it was willing to pay was limited to this amount of over-funding. Adinolfi Decl., at ¶¶ 16-17. Thus, six years after this dispute began, Alitalia for the first time indicated that its settlement proposal was limited to a source of funds which it was not even aware of until 1997 and which it had not specifically quantified until August 1999.

Prior to the August 19 meeting, Alitalia was willing to use and would have used financial resources other than the over-funding to pay for the cost of its proposals. Had Alitalia, in good faith, added the value of the over-funding to the value of its August 5 offer, the company would have bridged, in large part, the difference between the parties. Indeed, during this meeting, as he had before, the IAM representative made it clear that the union was willing to accept a severance package which was indistinguishable from those the IAM had reached with other foreign flag carriers that had also outsourced IAM work to sub-contractors. Adinolfi Decl., at ¶ 17.

As a result of Alitalia's bad faith, negotiations broke off on August 19. It is apparent that Alitalia engaged in a series of actions to forestall meaningful negotiations in the hope that the Department would approve the application even though the airline's dispute with the IAM was still unresolved. Simple union proposals have taken weeks for Alitalia to review. The airline has been unwilling to negotiate over its own proposals based upon an asserted lack of information which it should have obtained months earlier. Instead of adding to the financing upon which it had

always relied, Alitalia is now only willing to use funds which are no more than a windfall to the airline. If the public interest is to be promoted and **Alitalia's** tactics and labor relations record are to be condemned, the Department must reject the Application.

Finally, if Northwest and **KLM** are permitted to form an alliance with Alitalia, the **IAM** intends to extend its picket line against Alitalia to the other two carriers. Adinolfi **Decl.**, at ¶ 19. Thus, if approved, Northwest's and **KLM's** alliance with Alitalia would result in operational disruptions which would frustrate the public interest.

CONCLUSION

For all of the reasons stated above, the Department of Transportation should deny the Application.

Respectfully submitted,



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Robert S. Clayman  
Guerrieri, **Edmond & Clayman**, P.C.  
1625 Massachusetts Avenue, N.W.  
Suite 700  
Washington, DC 20036  
(202) 624-7400

Allison Beck, Esq.  
General Counsel  
International Association of  
Machinists and Aerospace  
Workers, AFL-CIO  
9000 Machinists Place  
Upper Marlboro, MD 20772-2687

Dated: August 23, 1999

**CERTIFICATE OF SERVICE**

I hereby certify that on this 23rd day of August, 1999, a true copy of the foregoing Answer Of The International Machinists And Aerospace Workers, AFL-CIO To The Joint Application was served by first-class mail, postage prepaid, on the persons named in the attached service list.

  
\_\_\_\_\_  
Robert S. Clayman

George J. Aste  
Vice President-International  
Affairs  
900 19th St., N.W., Suite 350  
Washington, DC 20006

Richard J. Fahy, Jr.  
Consulting Attorney  
900 19th St., N.W.  
Suite 350  
Washington, DC 20006

Kathleen A. Soled  
Sr. Vice President  
& General Counsel  
One City Centre, 18th Fl.  
515 N. Sixth St.  
St. Louis, MO 63101

Richard D. Mathias  
Zuckert, **Scoutt** & Rasenberger,  
LLP  
888 17th St., N.W., Suite 600  
Washington, DC 20006

Robert E. Cohn  
Shaw, **Pittman**, Potts  
& Trowbridge  
2300 N St., N.W.  
Washington, DC 20037

Lawrence M. **Nagin**  
Executive Vice President/  
General Counsel  
**USAirways**, Inc.  
Crystal Park Four  
2345 Crystal Drive  
Arlington, VA 22227

**Megan** Rae Poldy  
Associate General Counsel  
Northwest Airlines, Inc.  
901 15th St., N.W., Suite 310  
Washington, DC 20005

Moffett B. Roller  
Roller & Bauer  
1020 19th St., N.W., Suite 400  
Washington, DC 20036

Robert P. Silverberg  
Bagileo, Silverberg & Goldman  
1101 30th St., N.W., Suite 120  
Washington, DC 20036

Stephen **Gelband**  
**Hewes, Gelband, Lambert**  
& Dann, P.C.  
1000 Potomac St., N.W.  
Suite 300  
Washington, DC 20007

R. Bruce Keiner, Jr.  
Crowell & Moring  
1001 Pennsylvania Ave., N.W.  
Washington, DC 20004

Elliot M. Seiden  
Vice President  
Law & Government Affairs  
David G. Mishkin  
Vice President  
International Affairs  
Northwest Airlines, Inc.  
901 15th St., N.W., Suite 310  
Washington, DC 20005

Paul Mifsud  
Vice President, Government  
& Legal Affairs  
KLM Royal Dutch Airlines  
2501 M St., N.W.  
Washington, DC 20037

Pierre Murphy  
One **Westin** Center  
2445 M St., N.W., Suite 260  
Washington, DC 20037

Marshall S. Sinick  
Squire, Sanders and Dempsey  
1201 Pennsylvania Ave., N.W.  
Suite 500  
Washington, DC 20004

Dennis N. Barnes  
Morgan, Lewis & Bockius  
1800 M St., N.W., Suite 600N  
Washington, DC 20036

Nathaniel P. Breed, Jr.  
Shaw, **Pittman**, Potts  
& Trowbridge  
2300 N St., N.W.  
Washington, DC 20037

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IN THE UNITED STATES DISTRICT COURT  
FOR THE EASTERN DISTRICT OF MICHIGAN  
SOUTHERN DIVISION

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UNITED STATES OF AMERICA,	)
	)
Plaintiff,	)
	)
v.	)
	)
NORTHWEST AIRLINES CORPORATION	)
and	)
CONTINENTAL AIRLINES, INC.,	)
	)
Defendants.	)
<hr/>	

Civil Action No. : 98-74611

**AMENDED COMPLAINT**

The United States of America, plaintiff, acting under the direction of the Attorney General, brings this civil action to obtain equitable and other relief, including an order directing defendant Northwest Airlines Corporation (“Northwest”) to divest the majority voting interest it has acquired in its competitor, defendant Continental Airlines, Inc. (“Continental”), and adjudicating the agreements pursuant to which Northwest acquired that voting interest to be unlawful under the antitrust laws.

Plaintiff filed its complaint in this action on October 23, 1998, at which time Northwest had not yet acquired a voting interest in Continental. Subsequent to the filing of the complaint, Northwest modified the terms of the final agreements relating to the acquisition -- purportedly to “obviate” the harm to competition alleged by plaintiff in its complaint -- and proceeded to acquire a majority voting interest in Continental. The modifications do not remedy the

anticompetitive effects of the acquisition, and plaintiff therefore files this Amended Complaint, alleging as follows:

1. Northwest is the fourth largest airline in the United States, and Continental is the fifth largest. Both are financially sound, profitable airlines.
2. Northwest and Continental compete on price and service in thousands of routes

throughout the United States. They compete for passengers by offering, among other things, promotional fares for leisure travel, frequent flyer rewards, passenger upgrades, airport and in-flight amenities, and volume discounts to businesses and other organizations. They compete against each other in additional areas as well, such as on-time performance, ticketing procedures, schedules, and customer service.

3. Northwest and Continental are each other's most significant competitor for airline passenger service on seven densely traveled routes between cities where they operate their hubs - Detroit, Memphis, and Minneapolis for Northwest; and Cleveland, Houston, and Newark for Continental. Over 3.6 million passengers travel these seven "hub-to-hub" routes each year, generating nearly \$375 million in passenger revenues. Northwest and Continental are also direct competitors for airline travel between thousands of other cities, and are each other's most important competitor in a significant number of markets they serve on a connecting basis.

4. Northwest has acquired voting control over Continental, as well as a share in Continental's profits. The acquisition diminishes substantially both Northwest's and Continental's incentives to compete against each other on the seven existing hub-to-hub routes, as well as on other routes. Further, it will deter Continental from offering new service in competition with Northwest, such as expansion by Continental of its Cleveland hub.

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5. Thus, as a result of Northwest's acquisition of voting control of Continental, consumers likely will pay higher prices and receive lower quality service for scheduled airline passenger service in the markets dominated by Northwest and Continental, and lose the benefit of new, competitive entry by Continental against Northwest.

I.  
JURISDICTION AND VENUE

6. This action is instituted pursuant to Section 15 of the Clayton Act, as amended, 15 U.S.C. § 25, and Section 4 of the Sherman Act, 15 U.S.C. § 4, to prevent and restrain violations of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 1 of the Sherman Act, 15 U.S.C. § 1.

7. A substantial portion of each defendant's revenues is derived from the sale and provision of scheduled airline passenger service between different states. The defendants are engaged in interstate commerce and in activities that substantially affect interstate commerce. The Court has jurisdiction over this action and over the defendants pursuant to Section 12 of the Clayton Act, 15 U.S.C. § 22, and 28 U.S.C. §§ 1331 and 1337.

8. Venue is proper in this district with respect to the defendants under 15 U.S.C. § 22 and 28 U.S.C. § 1391(c), in that each of them is a corporation that transacts business and is found in the Eastern District of Michigan.

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II.  
DEFENDANTS

9. Defendant Northwest is a corporation organized and existing under the laws of

Delaware, with its principal offices in St. Paul, Minnesota. Northwest is the fourth largest airline in the United States, reporting total revenues of \$10.2 billion in 1997.

10. Defendant Continental is a corporation organized and existing under the laws of Delaware, with its principal offices in Houston, Texas. Continental is the fifth largest passenger airline in the United States, with total revenues of \$7.1 billion in 1997.

III.

THE ACQUISITION AND RELATED AGREEMENTS

11. On January 25, 1998, Northwest entered into an agreement with Air Partners, L.P. (“Air Partners”) and certain of its affiliates for the purpose of acquiring over fifty percent of the voting power over Continental (the “Investment Agreement”). On March 2, 1998, Northwest entered into an agreement with Barlow Investors III, LLC to purchase approximately 5 percent of the voting power over Continental (the “Barlow Purchase Agreement”) to ensure Northwest would own over 50 percent of the fully diluted voting power over Continental.

12. Northwest and Air Partners amended the Investment Agreement on March 2, 1998, April 24, 1998 and November 20, 1998. Pursuant to the November 20, 1998 amendment, the percentage of voting power Northwest was to acquire from Air Partners was reduced to about 46 percent. Notwithstanding the November 20, 1998 amendment to the Investment Agreement, the Barlow Purchase Agreement ensured that Northwest would own more than 50 percent of the

fully diluted voting power over Continental. Northwest consummated the Investment Agreement and the Barlow Purchase Agreement on November 20, 1998.

13. Under both the Investment Agreement and the Barlow Purchase Agreement, Northwest bargained for and obtained Continental Class A Shares, which carry super-voting rights.

14. As Class A stock, the shares purchased by Northwest from Air Partners and Barlow represent about 14 percent and 1 percent, respectively, of the total outstanding equity of Continental, but carry 46 percent and 5 percent, respectively, of the voting power over Continental.

15. Between entering the Investment Agreement on January 25, 1998, and the closing of the Investment and Barlow Purchase Agreements on November 20, 1998, Northwest, Continental and Air Partners entered into various agreements and adopted various plans that purport to govern how Northwest will exercise its voting control over Continental during the next ten years. These agreements and plans include the Governance Agreement (and its amendments), the Supplemental Agreement, the Voting Trust Agreement, and a shareholders’ rights agreement (hereinafter collectively referred to as the “Governance Agreements”).

16. Notwithstanding the Governance Agreements, Northwest now owns, and will continue to own, voting control of Continental. The Governance Agreements allow Northwest to retain at all times an ability to influence Continental’s management decisions -- such as through discussions with Continental directors, officers and employees, comments about Continental’s performance or management, or merely the ownership of Continental stock -- and eventually to exercise full control over Continental.

17. The Governance Agreements do not divest Northwest of ownership of its Continental stock. Rather, they merely impose certain restrictions on Northwest's exercise of its voting control during the first six years of its ownership of Continental and different, less restrictive, limitations on that exercise of voting control during years seven through ten. Northwest and Continental can agree privately at any time to eliminate any or all of these restrictions; in any event, all contractual limitations on Northwest's exercise of control over Continental expire no later than the tenth anniversary of the acquisition.

18. Under the Governance Agreements, Northwest retains its ownership of over 50 percent of the voting power over Continental and significant rights in and influence over Continental during the first six years of its ownership of Continental, including interalia:

- a. Northwest is free to direct the voting power of all its stock on key decisions that affect the future competitiveness of Continental, including major stock issuances, mergers, reorganizations, share exchanges, consolidations, or business combinations of Continental, as well as the sale of all or substantially all of Continental assets to any other company;
- b. No other shareholder can acquire voting control of Continental without the acquiescence of Northwest;
- c. In contested elections for the board of directors of Continental, Northwest can direct the vote of its controlling shares in support of the incumbent board's recommendations;
- d. In all elections for the board of directors of Continental, Northwest can register a public vote of no confidence in Continental management by

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directing its vote against certain directors, including Continental managers seeking election or re-election to the board;

- e. In addition to the approximately 51 percent of the voting power of Continental it owns, Northwest has the right to direct the vote of certain additional shares owned by 1998 CAI Partners, L.P. ("CAIP"). The CAIP shares represent approximately 5 percent of the voting power over Continental. The CAIP shares must be voted as directed by Northwest on key matters such as mergers and changes to Continental's by-laws. Northwest also can direct that the CAIP shares be voted as recommended by Continental's board in the election of directors, if that is how Northwest chooses to vote its own shares.

19. In addition to the rights that it retains during the first six years of its ownership of voting control over Continental, Northwest obtains even greater rights and influence under the Governance Agreements during years seven through ten of its ownership:

- a. Northwest can vote 20 percent of the voting power of Continental on any issue presented to shareholders, including executive compensation;
- b. Northwest can nominate, solicit support for, and vote for its own representatives to serve on Continental's board of directors.

20. When the Governance Agreements expire, Northwest can fully exercise its voting control over Continental.

21. As a result of the Investment Agreement, the former owners of Air Partners hold voting shares of Northwest. The Investment Agreement grants these former Air Partners owners,

through Coulco, Inc., the right to designate one individual to sit on the board of Northwest. Coulco is owned by James Coulter who, together with David Bonderman, controlled the general partner in Air Partners. The Investment Agreement requires that the Coulco designee be acceptable to Northwest, and the agreement identifies James Coulter and William S. Price as acceptable designees.

22. The Investment Agreement is likely to create interlocking directors on the boards of directors of Northwest and Continental. William S. Price currently sits on the Continental board, and if he is elected to the Northwest board, the two airlines will have a common director. In addition to Price, three other individuals formerly affiliated with Air Partners currently sit on the Continental board: David Bonderman, Thomas Barrack, and Donald Sturm. Former Air Partners owners retain through CAIP about 5 percent of the voting power of Continental. If Coulter, Price, or any other person formerly affiliated with Air Partners is designated to the Northwest board, the former Air Partners owners will have representatives on the boards of both Northwest and Continental.

23. Northwest and Continental also have entered into an alliance agreement (the "Alliance Agreement"), which provides for system-wide joint marketing of the two carriers' services. Consummation of the Alliance Agreement is not contingent upon consummation of the Investment Agreement. Although such alliance agreements between airlines have become common in recent years, it is uncommon for such alliances to be accompanied by substantial equity ownership. Few, if any, have involved a majority interest. Both Northwest and Continental have alliances with other domestic and foreign carriers, but none involves voting control by one partner of the other.

#### IV.

#### THE RELEVANT MARKETS

24. For the vast majority of passengers who wish to travel between various origin and destination ("O&D") airports or cities in the United States, there is no other mode of transportation they would substitute for scheduled airline passenger service in response to a significant fare increase for scheduled airline passenger service. Scheduled airline passenger service, therefore, constitutes a line of commerce and a relevant product market within the meaning of Section 7 of the Clayton Act, and within the meaning of Section 1 of the Sherman Act.

25. Few passengers currently flying nonstop between specific O&D airports or cities in the United States would substitute connecting service (i.e., flights with one or more stops en route) for nonstop service in response to a significant fare increase for nonstop scheduled airline passenger service. Nonstop scheduled airline passenger service, therefore, constitutes a line of commerce and a relevant product market within the meaning of Section 7 of the Clayton Act, and within the meaning of Section 1 of the Sherman Act.

26. With respect to both scheduled airline passenger service and nonstop scheduled airline passenger service, few passengers who wish to fly between specific O&D airports or cities in the United States would switch to flights between other airports or cities in response to a

significant fare increase. Specific O&D airports or cities (“city pairs”), therefore, constitute a section of the country and a relevant geographic market with the meaning of Section 7 of the Clayton Act, and within the meaning of Section 1 of the Sherman Act.

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V.  
CONCENTRATION AND ENTRY

27. Northwest and Continental are among the ten largest airlines in the world. Within the United States, Northwest and Continental compete for passengers in thousands of city-pair markets.

28. Northwest operates hubs at airports in Detroit, Michigan; Minneapolis/St. Paul, Minnesota; and Memphis, Tennessee.

29. Continental operates hubs at airports in Newark, New Jersey; Cleveland, Ohio; and Houston, Texas.

30. Under the “hub and spoke” system, an airline concentrates passengers from many points at the “hub” location and then provides nonstop service from the hub airport to a large number of destinations (the “spokes”). The hub and spoke system allows a carrier to serve more city pairs with more frequencies than would be profitable without the use of a hub.

31. In seven hub-to-hub city pair markets, Northwest and Continental together dominate the market for nonstop service and for all scheduled airline passenger service. These markets are Detroit-Cleveland, Detroit-New York (including Newark), Detroit-Houston, Cleveland-Minneapolis, Minneapolis-New York (including Newark), Houston-Minneapolis, and Houston-Memphis. Northwest and Continental’s market shares for nonstop flights in each of the seven markets are:

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**Northwest/Continental Hub-to-Hub Nonstop Shares**

<b>Route</b>	<b>NW Share of Nonstop Flights</b>	<b>CO Share of Nonstop Flights</b>	<b>Combined NW &amp; CO Share of Nonstop Flights</b>
Detroit-Cleveland	52%	41%	93%
Detroit-New York	69%	14%	83%
Detroit-Houston	36%	64%	100%
Cleveland-Minneapolis	53%	47%	100%
Minneapolis-New York	80%	20%	100%
Houston-Minneapolis	42%	58%	100%
Houston-Memphis	39%	61%	100%

32. In two other hub-to-hub routes, Memphis-Newark and Cleveland-Memphis, Northwest currently has a nonstop monopoly. As the only airline with hubs in Newark and Cleveland, Continental is the most likely potential entrant to challenge Northwest's nonstop monopoly. After plaintiffs complaint was filed, Continental announced it would begin nonstop service on the Memphis-Newark route beginning in February 1999.

33. In total, nearly four million passengers travel in these nine hub-to-hub city pairs annually, generating revenues of nearly \$400 million per year.

34. Effective new entry for the provision of nonstop service in the hub-to-hub markets is unlikely by any carrier without a hub at one of the endpoints of the city pair. A hub carrier, such as Northwest or Continental, has significant cost advantages over a non-hub carrier attempting to offer service originating at the hub airport. Building a competing hub in the same city would require considerable time and investment, and is not likely to occur in response to fare increases in the hub-to-hub markets at issue here.

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35. Other factors impede new entry, including difficulty in obtaining access to gate facilities; the effects of travel agent incentive programs offered by dominant incumbents; frequent flyer programs; and the risk of aggressive responses to new entry by the dominant incumbent carrier serving a particular market.

36. In addition to the hub-to-hub routes where Northwest and Continental share a virtual duopoly, Northwest and Continental have a large share of the passengers traveling on connecting flights in numerous city pair markets. Because of the light traffic on these routes and the short flights to the Northwest or Continental hubs, carriers with more distant hubs are unlikely to initiate or expand competitive service to these destinations through their own hubs in response to significant fare increases.

## VI.

### ANTICOMPETITIVE EFFECTS

37. Northwest's ownership of a controlling interest in Continental will reduce Continental's incentive to compete aggressively against Northwest. Furthermore, Northwest's more than fourteen percent equity stake in Continental's profits, plus its ability to merge in the

future with Continental, will reduce Northwest's incentive to compete aggressively against Continental.

38. Northwest's ownership of a controlling interest in Continental will diminish actual competition in seven hub-to-hub markets and numerous other markets that already are concentrated. It also will diminish the potential for nonstop competition for Memphis-Cleveland and Memphis-Newark, as well as potential competition in other markets for which Northwest

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and Continental are among the few likely future providers of scheduled airline passenger service. As a result, fares likely will increase and service likely will decrease in these city pairs.

39. Northwest's ownership of a controlling interest in Continental also will reduce the likelihood that Continental will initiate nonstop service from its hubs, such as Cleveland, to cities already served by Northwest through its hubs, such as Detroit.

40. The Governance Agreements do not prevent the harm likely to result from Northwest's ownership of a controlling interest in Continental. First, no privately negotiated agreement can alter the fact that Northwest retains ownership of its Continental stock, and Continental will not compete vigorously with its owner during the terms of the Governance Agreements. Second, even under the Governance Agreements, Northwest (a) may engage in "discussions with directors, officers and employees" of Continental; (b) retains direct control over key Continental strategic decisions at all times; and (c) retains significant influence over Continental's board of directors and management.

41. Northwest's ability to exercise the direct control attendant to its ownership interests increases in years seven through ten following the acquisition, even if the Governance Agreements remain in place. Those agreements may expire earlier by their own terms and, like all agreements between two parties, the Governance Agreements can be amended or revoked at any time by the parties -- Continental and its competitor and new owner, Northwest.

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## VII. VIOLATIONS ALLEGED

42. The effect of Northwest's ownership of voting power over Continental may be substantially to lessen competition in interstate trade and commerce in violation of Section 7 of the Clayton Act, and to unreasonably restrain trade in violation of Section 1 of the Sherman Act in the following ways, among others:

- a. Actual and potential competition between Northwest and Continental for nonstop scheduled airline passenger service in the hub-to-hub markets will be reduced or eliminated;
- b. Actual and potential competition between Northwest and Continental for scheduled airline passenger service in city-pair markets where Northwest and Continental are dominant providers of connecting service will be reduced or eliminated;
- c. Competition generally in numerous city-pair markets for scheduled airline passenger service may be lessened substantially;
- d. Coordinated pricing activity between providers of scheduled airline

- passenger service likely will be facilitated; and
- e. Prices for scheduled airline passenger service in numerous concentrated city-pair markets in the United States are likely to increase.
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IX.  
REQUEST FOR RELIEF

WHEREFORE, Plaintiff prays:

1. That a permanent injunction be issued preventing and restraining defendant Northwest and all persons acting on its behalf from owning or holding voting stock in Continental, or any of Continental's affiliates or subsidiaries, and directing that Northwest divest promptly all voting stock in Continental on such terms and conditions as may be agreed to by plaintiff and the Court;
2. That the Investment Agreement between Northwest and Air Partners and the Barlow Purchase Agreement between Northwest and Barlow be adjudged to be in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18, and Section 1 of the Sherman Act, 15 U.S.C. § 1;
3. That plaintiff have such other and **further** relief as the nature of this case may require and as is just and proper, including modifications to the Governance Agreements between Northwest, Continental and Air Partners as appropriate; and
4. That Plaintiff recover the costs of this action.

DATED this 18th day of December 1998.

\_\_\_\_\_/s/\_\_\_\_\_  
JOEL I. KLEIN  
Assistant Attorney General

\_\_\_\_\_/s/\_\_\_\_\_  
SAUL A. GREEN  
United States Attorney

\_\_\_\_\_/s/\_\_\_\_\_  
JOHN M. NANNES  
Deputy Assistant Attorney General

\_\_\_\_\_/s/\_\_\_\_\_  
JULIA C. PIDGEON  
Assistant United States Attorney  
Pa. Atty. Lic. 37949  
211 W. Fort Street, Suite 200 1  
Detroit, Michigan 48226  
(313) 226-9772

\_\_\_\_\_/s/\_\_\_\_\_  
CONSTANCE K. ROBINSON  
Director of Operations and Merger  
Enforcement

\_\_\_\_\_/s/\_\_\_\_\_  
ROGER W. FONES  
Chief, Transportation, Energy and  
Agriculture Section

\_\_\_\_\_/s/\_\_\_\_\_  
DONNA N. KOOPERSTEIN  
Assistant Chief, Transportation, Energy  
and Agriculture Section

\_\_\_\_\_/s/\_\_\_\_\_  
JILL PTACEK  
MICHAEL BILLIEL  
JOHN READ  
DOROTHY FOUNTAIN  
TRACEY CHAMBERS  
SALVATORE MASSA  
Attorneys  
United States Department of Justice  
Antitrust Division  
Transportation, Energy and  
Agriculture Section  
325<sup>th</sup> Street, N.W., Suite 500  
Washington, D.C. 20530

BEFORE THE  
DEPARTMENT OF TRANSPORTATION  
OFFICE OF THE SECRETARY

\_\_\_\_\_  
Joint Application of )  
 )  
ALITALIA-LINEE AEREE **ITALIANE-** )  
**S.p.A.** )  
and )  
KLM ROYAL DUTCH AIRLINES ) Docket OST-99-5674  
and )  
NORTHWEST AIRLINES, INC. )  
 )  
for approval of and antitrust )  
immunity for agreements pursuant )  
to 49 U.S.C. §§ 41308 and 41309 )  
\_\_\_\_\_ )

**DECLARATION OF JOSEPH ADINOLFI**

Joseph Adinolfi hereby declares, in accordance with 28 U.S.C. § 1746, as follows:

1. Since 1986 I have served as a General Chairman of District Lodge 142 of the International Association of Machinists and Aerospace Workers, AFL-CIO ("IAM"). My responsibilities in this position include administering and negotiating collective bargaining agreements for **IAM-represented** employees at various airlines, including Alitalia Airlines ("**Alitalia**").

2. Since 1952, the **IAM** has represented employees of Alitalia and currently represents those employees who work in the traffic (passenger service), cargo and reservations departments.

3. In August 1990, negotiations began between Alitalia and the **IAM** to amend the then current collective bargaining agreement. I assumed principal responsibility for these negotiations in 1992.

4. On September 2, 1993, Alitalia representatives presented **IAM** negotiators with what the company termed its "**last best offer.**" This exchange took place at the end of the negotiations process under the Railway Labor Act. Pursuant to those procedures, if an agreement was not reached by midnight on September 2, each party could resort to self-help -- the **IAM** could strike the carrier and Alitalia could unilaterally impose terms and conditions of employment.

5. The **IAM** representatives asked the federally-appointed mediator to convene a meeting so that the parties could discuss **Alitalia's** proposal. Shortly thereafter, the mediator informed the **IAM** that Alitalia was unwilling to meet over their "**last best offer.**" Negotiations then ended.

6. Although the **IAM** negotiating committee did not endorse **Alitalia's** proposal, based upon the **IAM's** policy, I intended to present this offer to the membership who would be given the opportunity to ratify or reject the offer, or vote to strike the airline. Accordingly, I scheduled a meeting for September 3 at noon at JFK International Airport at which time I would explain the proposal and present it to the **IAM** membership for both a ratification and strike vote.

7. Upon arriving at the meeting, I was met by an large group of Alitalia employees who were visibly upset because Alitalia had decided to lock out all **IAM-represented** employees. Cargo employees who work the midnight shift reported that, upon arriving at the airport gate, they were met by security guards hired by Alitalia,

who informed them that they would not be allowed to enter **Alitalia's** premises or report to work. The day shift of cargo employees was similarly barred from working. The traffic employees, who were scheduled for the morning shift on September 3, worked for approximately two hours, when an Alitalia representative told them that they could not continue their shift and would have to leave.

8. Based upon my experience as a General Chairman for 13 years and a union representative for the past 25 years, **Alitalia's** conduct constituted a lock-out. At that point, the **IAM** had not initiated any strike or job action and the employees' inability to perform their jobs was purely the result of Alitalia preventing them from doing so.

9. Several days later, the manager of **Alitalia's** cargo department, Bruno Sabbatini, sent each cargo and traffic employee a letter dated September 3 stating that "the Company did not lock-out anyone" and that the employees could return to work. See Attachment 1. Immediately after receiving a copy of this letter, I telephoned Mr. Sabbatini to confirm, if, in fact, the **IAM**-represented employees could return to their jobs. He told me the Company would not allow the employees to return to work. Alitalia contracted out the cargo work to non-union contractors and imported Italian nationals to replace ticket-counter employees, permanently replacing 150 **IAM** members.

10. Ultimately, the **IAM** membership voted to reject the company's proposal and voted to strike the airline. The **IAM**

declared a strike against the airline which continues today. **IAM-**represented employees have manned a picket line virtually every day since September 3, 1993, and are committed to remain on that line until there is a just resolution of this dispute.

11. Since the September 1993 lock-out, the carrier has sporadically agreed to meet, but on each occasion when a negotiation session has been held, little or no progress has been made.

12. In late 1997, the **IAM** apprised Alitalia that the Union Pension Plan may be over-funded and that if a surplus existed it could provide Alitalia with an additional source of money for settling this dispute.

13. In May 1999, the **IAM** sought the assistance of Northwest Airlines to resolve this dispute and, as part of that effort, Northwest helped to schedule a meeting of the **IAM** and Alitalia on July 6, 1999.

14. The parties met and the **IAM** provided Alitalia with an offer which would resolve all outstanding issues. **Alitalia's** representatives stated that they needed time to review the offer and wanted to schedule another meeting. A second meeting was set for two days, August 5 and 6, in order to provide the parties ample time to negotiate and conclude an agreement.

15. On August 5, Alitalia made a proposal, the two core components of which were a severance package worth approximately \$1.9 million and an offer to improve the pension benefits of the **IAM-represented** employees. **Alitalia's** representatives explained

that it had not yet calculated the amount of over-funding in the pension **plan** and that this figure was critical to making a definitive proposal on pension improvements. This meeting was the first time Alitalia indicated that it intended to use the over-funding as a source of monies to resolve its dispute with the **IAM**. **Alitalia's** representatives did not explain why they had not calculated the amount of over-funding prior to this meeting.

16. At the August 5 meeting, more than eighteen months after being apprised of this potential source and four weeks after our July meeting, Alitalia announced that it would not entertain any counter-offers from the **IAM** until it had determined the amount of over-funding. Its representatives stated that this computation would not be completed for another week and so the parties agreed to resume negotiations on August 19. On August 17, **IAM** representatives received a report from **Alitalia's** actuary that the amount of over-funding in the Union Pension Plan was \$2.7 million.

17. At the August 19 meeting, Alitalia stated that the total settlement amount it was willing to pay was limited to the \$2.7 million of over-funding. During this meeting, I made it **clear, as I had at** other negotiation sessions, that the **IAM** was willing to **accept a** severance package that was essentially the same as those **the IAM had** reached with other foreign flag carriers that had **sub-contracted out IAM** work.

18. I am not aware of any other dispute between an airline and the **IAM** which has lasted as long as the one with Alitalia. No **other airline has** resorted to a lock-out of **IAM-represented**

employees. In every other case where the **IAM** has been in negotiations with a foreign flag carrier, it has been able to reach an agreement.

19. I understand that on May 11, 1999, Alitalia, KIM and Northwest submitted an application to the Department of Transportation to form an alliance. The application makes it clear that the three airlines intend to operate as a single entity. It is my understanding that the **IAM** intends to treat them as such and will, accordingly, extend its picket line against Alitalia to Northwest and KIM.

I declare under penalty of perjury that the foregoing is true and correct. Executed on August 20, 1999.

  
Joseph Adinolfi



September 3, 1993

This is to inform you that the Company did not lock-out anyone.

Therefore, you are welcomed back to work.

Bruno Sabbatini  
Cargo Traffic and  
Operations Manager