DEPT. OF TRANSPORTATION
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BEFORE THE

DEPARTMENT OF TRANSPORTATION

WASHINGTON, D. C.

Joint Application of

AMERICAN AIRLINES, INC. and
EXECUTIVE AIRLINES, INC., FLAGSHIP
AIRLINES, INC., SIMMONS AIRLINES,
INC., and WINGS WEST AIRLINES, INC.
(d/b/a AMERICAN EAGLE)
and
CANADIAN AIRLINES INTERNATIONAL LTD.
and ONTARIO EXPRESS LTD. and TIME AIR
INC. (d/b/a CANADIAN REGIONAL) and
INTER-CANADIEN (1991) INC.

under 49 USC 41308 and 41309 for approval
of and antitrust immunity for commercial
alliance agreement

OST-95-792 -32

JOINT ANSWER OF AMERICAN AIRLINES, INC. et al.
AND CANADIAN AIRLINES INTERNATIONAL LTD. et al.
TO COMMENTS ON SHOW-CAUSE ORDER 96-5-38

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June 7, 1996

BEFORE THE

DEPARTMENT OF TRANSPORTATION

WASHINGTON, D. C.

Joint Application of AMERICAN AIRLINES, INC. and EXECUTIVE AIRLINES, INC., FLAGSHIP AIRLINES, INC., SIMMONS AIRLINES, INC., and WINGS WEST AIRLINES, INC. (d/b/a AMERICAN EAGLE) and CANADIAN AIRLINES INTERNATIONAL LTD. and ONTARIO EXPRESS LTD. and TIME AIR INC. (d/b/a CANADIAN REGIONAL) and INTER-CANADIEN (1991) INC. under 49 USC 41308 and 41309 for approval of and antitrust immunity for commercial alliance agreement	OST-95-792

JOINT ANSWER OF AMERICAN AIRLINES, INC. ~~et al.~~
AND CANADIAN AIRLINES INTERNATIONAL LTD. ~~et al.~~
TO COMMENTS ON SHOW-CAUSE ORDER 96-5-38

American Airlines, Inc. and its regional affiliates, and Canadian Airlines International Ltd. and its regional affiliates, hereby answer the comments filed on June 4, 1996 by Continental Airlines, Inc., Trans World Airlines, Inc., United Air Lines, Inc., and Air Canada in response to show-cause Order 96-5-38, May 28, 1996. By that order, the Department tentatively granted approval of and antitrust immunity for the Commercial Alliance Agreement between American and Canadian.

The Department made this determination because it found that "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 American to compete more effectively with other carriers and alliances in the U.S.-Canada transborder markets. With our proposed limitation of approval and immunity to these transborder markets, our proposed actions 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" (p. 2).

The Department should promptly make final the tentative findings and conclusions in Order 96-5-38. None of the comments or objections justifies denying or delaying the public benefits that will result from the joint services to be offered by American and Canadian under their alliance agreement.

1. Continental

Pursuant to the Department's scheduling notice in Order 96-l-6, January 11, 1996, answers to the American/Canadian joint application were due on February 6, 1996. Answers were submitted by Delta Air Lines, Inc., Northwest Airlines, Inc., United Air Lines, Inc., Air Canada, and the International Air Transport Association. Continental did not file an answer, and had never voiced any objection to the

application until the date for responses to the show-cause order tentatively granting approval. Accordingly, Continental's statement that the five-day period allowed for responding to the show-cause order Violates carrier rights to due process" (p. 2 n. 3) is without substance. Continental had more than three months -- from November 3, 1995 to February 6, 1996 -- to answer the joint application, and chose not to do so.

Moreover, it is clear that Continental's dilatory objections have nothing to do with principle. Continental has obviously decided to object now because its own hoped-for alliance with Air Canada has fallen through, as evidenced by the United/Air Canada joint immunity application filed on June 4, 1996 (OST-96-1434).

In any event, while we question Continental's standing to raise objections to the show-cause order when it failed to answer the application initially, Continental has not presented any good reason for the Department to reverse its tentative findings and conclusions in favor of approving and immunizing the American/Canadian alliance.

Order 96-5-38 thoroughly explains the unique circumstances of the U.S.-Canada market, and why the short-term phase-in provisions of the U.S.-Canada open skies agreement do not warrant withholding immunity. As the Department found,

> "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. It is not surprising that these characteristics have created a demand for transborder air services that dwarfs all other bilateral markets. It 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" (p. 10).

The Department went on to say that it had weighed the arguments of both Delta and Northwest -- which were similar to the objections now being made by Continental -- that the U.S.-Canada relationship "lacks some attributes of a full comprehensive open-skies agreement" (p. 10). While the Department said that it agreed with these arguments as a matter of principle, "we view this application as a unique exception to that principle, given the very distinct character of the U.S.-Canada market. 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 conclusion of the brief phase-in of entry and capacity at Montreal, Toronto, and Vancouver, the underlying air transport agreement between the United States and Canada will have created an open environment

for transborder passenger and belly cargo services and prices" (id.).

Order 96-5-38 also addresses in detail the competitive situation at Toronto, and in the New York-Toronto market in particular, which is the focus of much of Continental's pleading. The Department noted that the U.S.-Canada Agreemeent, "even for Toronto, currently provides certainty of the lifting of all the restrictions at these cities [Toronto, Vancouver, and Montreal] in only a brief period, during which no competitive harm from the alliance can be foreseen," especially since Canadian "is a relatively small operator in the Canadian markets," whereas Air Canada "dominates the overall Montreal and Toronto markets" (p. 15).

The Department carefully analyzed the structure of the U.S.-Canada accord, and fully explained the reasons for its proposed decision in favor of immediate immunity for the American/Canadian alliance:

> "We have tentatively concluded that despite our policy not to grant antitrust immunity in markets where there are restrictions on entry or flexibility of operations, the unique situation arising from the U.S.-Canada agreement, as recited above, and the limited nature of the continuing restrictions, balanced against the very significant consumer competitive advantages that will arise form this alliance, justifies our grant of approval and immunity in these markets, notwithstanding the restrictions temporarily in effect.

* * *

> "To reiterate, 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 four new U.S. carrier designations made available in February 1997 will satisfy most U.S. carrier requests to serve that market, and that, except with respect to the New York-Toronto market, the market will effectively be open during the interim period before de iure open skies. Second, we rely on the fact that under the U.S.-Canada bilateral, an open transborder aviation environment will become effective automatically, without any further action by any government entity in February, 1998. * * * Moreover, we note that Air Canada has a 41.2 percent market share of transborder passengers at Toronto. We would not want to harm competition by artificially delaying the competitive entry of a strong alliance. These factors are relevant to our decision to accelerate the grant of antitrust immunity in this case and not to allow by inaction a result that is less competitive" (pp. 14, 15).

In short, despite the fact that Continental failed to object to the American/Canadian application on the answer date in February, the Department has already thoroughly responded to the arguments Continental has raised, because similar arguments were made by Delta and Northwest (and neither of them has objected to the show-cause order). Those arguments are all predicated on the formalistic notion that the U.S.-Canada agreement must meet some inflexible model before antitrust immunity can be granted, even where, as found by the Department here, a failure to grant immunity would reduce competition.

To say, as Continental does, that the U.S.-Canada accord failed to achieve open skies truly exalts form over

substance. As Secretary Pena stated shortly after the first anniversary of the new agreement, "[f]lights are up 40 percent. There are 45 new routes. Fourteen U.S. cities, which never had service now have nonstop service to Canada. In total, Americans can take nonstop flights from 34 different U.S. cities to get to Canada." See Remarks before the Federal Aviation Administration Forecast Conference, March 5, 1996, p. 3. None of the other bilateral agreements the U.S. has recently concluded has succeeded in opening up the skies in fact to the extent that the agreement with Canada has.

Finally, Continental's charge that antitrust immunity for the American/Canadian alliance would lessen competition is far wide of the mark. Immunity for American and Canadian will enhance their ability to compete with the dominant carrier in the transborder market, Air Canada. We also note that the Department of Justice has fully accepted the terms of the Department's tentative order.

The proposed approval of and antitrust immunity for the American/Canadian alliance, based on the unique circumstances of the U.S.-Canada open skies agreement, and the unique characteristics of the transborder market, is well-founded as a matter of both fact and policy. The show-cause order should promptly be made final, notwithstanding Continental's untimely objections.

2. **TWA**

TWA, like Continental, failed to file an answer to the joint application on the February 6, 1996 date established by the Department. While TWA now states that it takes no position on the merits of the American/Canadian alliance, it urges that the final order be conditioned so that immunity will automatically terminate if potential competitors "are blocked by either governmental or marketplace restrictions in the foreign country" (p. 3). Alternatively, TWA urges that the Department "establish ground rules for carriers to file requests for removal of immunity" (p. 4).

TWA has presented no good basis for the Department to impose such conditions -- which do not appear in any other immunity order[1] -- on American and Canadian. Indeed, TWA opposed the grant of immunity in both the United/Lufthansa and Delta/Swissair/Sabena/Austrian proceedings, but made no mention of any need for such conditions there. It would be unwarranted and discriminatory to single out the American/Canadian transaction for disparate treatment, and the Department should decline to do so.

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[1]See Order 93-l-11, January 8, 1993 (Northwest/KLM); Order 96-5-27, May 21, 1996 (United/Lufthansa); Order 96-5-26 (show-cause), May 21, 1996 (Delta/Swissair/Sabena/Austrian).

3. United and Air Canada

On June 4, 1996 -- the day for comments or objections to Order 96-5-38 tentatively approving and granting antitrust immunity to the American/Canadian alliance -- United and Air Canada submitted a joint application for approval and immunity of their own alliance (OST-96-1434). In their accompanying comments here, they state that they have no objection to the American/Canadian alliance, provided that their joint application is also granted.

The United/Air Canada application should be processed by the Department in due course. The suggestion that a final decision on the American/Canadian application should be deferred, and that the two applications should be consolidated for contemporaneous consideration, is entirely without merit. The American/Canadian application was filed on November 3, 1995, and has now been pending for more than seven months. Had United's and Air Canada's real objective been simultaneous review, they would have submitted the appropriate application long ago.

The fact that United and Air Canada filed their own request on the very day that comments were due on the American/Canadian show-cause order surely does not give rise to

legitimate Ashbacker claims.[2] Indeed, to condone the tactics of United and Air Canada would set a most undesirable precedent. Opposing parties could seek to delay a competitor's application indefinitely simply by opposing it on the merits, as United and Air Canada did here, and then reverse course and file "me too" applications when their opposition fails.

Such gamesmanship with the Department's procedures should not be allowed. The Department should promptly make the show-cause order final, and separately process the United/Air Canada application submitted three days ago.

CONCLUSION

In Order 96-5-38, the Department tentatively concluded that granting the American/Canadian application for approval of and antitrust immunity for their Commercial Alliance 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" (p. 23). The Department should enter

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[2] See, e.g., Flvins Tiger Transpacific Renewal Case, 75 CAB 107, 108 (1977) (rejecting United's Ashbacker arguments as not "timely presented" where United failed to file a competing application at the proper stage of the proceeding).

its final order granting approval and immunity without delay, so that the public may receive all of the benefits that the American/Canadian alliance will bring to the transborder market.

Respectfully submitted,

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June 7, 1996

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing answer by fax or first-class mail on all persons named on the service list in this proceeding.

CARL B. NELSON, JR.

June 7, 1996