

# CONTINENTAL JOINS THE (ALL)STAR ALLIANCE: ANTITRUST CONCERNS WITH AIRLINE ALLIANCES AND OPEN-SKIES TREATIES

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## I. INTRODUCTION

On October 27, 2009 Continental Airlines switched from the Delta-dominated SkyTeam Alliance to partner with United Airlines in the Star Alliance.<sup>1</sup> The move was praised by many, but criticized by some as the equivalent of collusion between competitors determined to concentrate international airline markets and destroy competition.<sup>2</sup> The United States has turned to “Open Skies agreements,” such as that entered into with the European Union in April 2007.<sup>3</sup> Open Skies agreements are negotiated with foreign nations and are aimed at alleviating anticompetitive concerns in the international aviation industry.<sup>4</sup>

The U.S.-E.U. agreement permits any U.S. or E.U. airline to fly freely between any city in the United States and any member state of the E.U.<sup>5</sup> The agreement, to be implemented in phases, claims to increase competition among carriers and open access to more international airports, enabling a competitive global

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1. Shannon Buggs, *Aligning the Airlines*, HOUS. CHRON., Sept. 23, 2009, at D1. The Author wrote this Article during the Fall of 2009. Since then, there have been significant changes in the airline industry, notably the merger of Continental and United Airlines. Nonetheless, the Author hopes this Article will remain a useful explanation of how the United States grants antitrust immunity to airlines and how this affects Open Skies treaties.

2. See Loren Steffy, Op-Ed, *Some Logic Only Flies in Airlineland*, HOUS. CHRON., Apr. 28, 2009, available at <http://www.chron.com/disp/story.mpl/business/steffy/6397854.html> (arguing that the alliance could harm consumers by increasing Star Alliance’s power to extract monopoly rents and increase barriers to entry for certain transatlantic markets).

3. Air Transport Agreement, U.S.-E.U., Apr. 30, 2007, 46 I.L.M. 470 [hereinafter U.S.-E.U. Open Skies].

4. See *Open Skies Agreements*, U.S. DEP’T OF STATE, <http://www.state.gov/e/eeb/tra/ata/> (last visited Feb. 26, 2011) [hereinafter DEP’T OF STATE] (discussing how such agreements allow for increased cooperation and enhanced access to markets for airlines).

5. Joe Sharkey, *Open Skies, Better Deals (for Now)*, N.Y. TIMES, Apr. 6, 2008, at BU 2.

market.<sup>6</sup> However, many feel that the agreement will only produce temporary benefits for international travelers, which may disappear with the implementation of Phase II at a later date.<sup>7</sup> Phase II will allow foreign airlines to own greater shares in U.S. airlines, a provision that the United States has said it may not accept.<sup>8</sup> This could lead to a highly concentrated global airline market, opening the door for monopolization or collusion by a few dominant carriers. Thus, any benefits to consumers under an Open Skies agreement would be undermined by the concentrated market.

This fear is enhanced by the recent trend in airline mergers and joint ventures, and the increased concentration of international airline alliances.<sup>9</sup> Airline alliances (i.e., Star, SkyTeam, and Oneworld) are agreements between domestic and foreign airlines allowing them to share revenues and coordinate prices, scheduling and code sharing (enabling baggage transfer on connecting flights).<sup>10</sup> Because foreign ownership of airlines is prohibited in the United States, as well as in many E.U. countries, airline alliances serve much of the same functions as a merger, only without the formality of transferring ownership rights.<sup>11</sup> In other industries, coordination of pricing and scheduling among top competitors would constitute collusion and a *per se* violation of section 1 of the Sherman Antitrust Act.<sup>12</sup> However, none of the three global alliances need to worry

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6. *Id.*

7. *Id.*

8. *Id.*

9. See Darren Bush, Op-Ed., *Abort the Takeoff on New Airline Mergers*, HOUS. CHRON., Oct. 21, 2007, at E5 (criticizing the consolidation of “major airlines” and the influx of federal bailout money into the airline industry).

10. James Reitzes & Diana Moss, *Airline Alliances & Systems Competition*, 45 HOUS. L. REV. 293, 294–95 (2008).

11. *Id.* at 294; Jacob A. Warden, Comment, “*Open Skies*” at a Crossroads: How the United States and European Union Should Use the ECJ Transport Cases to Reconstruct the Transatlantic Aviation Regime, 24 NW. J. INT’L L. & BUS. 227, 227 (2003).

12. See *Broadcast Music, Inc. v. Columbia Broadcasting Sys., Inc.*, 441 U.S. 1, 8, 19–20 (1979) (recognizing that some agreements, on their face, “always or almost always tend to restrict competition and decrease output,” and thus are *per se* illegal under § 1 of the Sherman Act). The Sherman Antitrust Act is the basic foundation of American competition law, which prohibits “monopolizing” and “every . . . combination . . . in restraint of trade or commerce.” 15 U.S.C. §§ 1–2 (2006).

about prosecution under the U.S. or E.U.'s antitrust laws: Oneworld, Star, and SkyTeam alliance members have all been granted antitrust immunity by the U.S. Department of Transportation (DOT) and the E.U.'s European Commission.<sup>13</sup>

Two of the major anticompetitive concerns created by immunized alliances are that they (1) eliminate horizontal competition among member carriers and, (2) encourage alliance-dominated hubs in both the United States and European Union.<sup>14</sup> Such effects undermine the principles of the U.S.-E.U. Open Skies Agreement, which is supposed to allow airlines to fly freely to any city within member states' boundaries.<sup>15</sup> More and more independent airlines around the world are essentially forced into an alliance just to gain access to alliance-dominated hubs so they can compete in the international market.<sup>16</sup> Meanwhile, the alliances themselves are happy to welcome additional members in order to extend their dominance into new international markets and to create new exclusive hubs.<sup>17</sup>

Another major concern is the United States' dominance of the global airline industry.<sup>18</sup> Before the trend toward Open Skies agreements, the major U.S. airlines were losing money and on the verge of bankruptcy due to the deregulation of the industry and overcapacity in domestic markets.<sup>19</sup> Foreign capital investment in U.S. airlines was severely limited by restrictions on foreign ownership.<sup>20</sup> To offset the problem of

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13. Aaron Karp, *DOT Gives Final Approval for Oneworld Antitrust Immunity*, AIR TRANSP. WORLD (July 21, 2010), <http://atwonline.com/international-aviation-regulation/news/dot-gives-final-approval-oneworld-antitrust-immunity-0720>.

14. Reitzes & Moss, *supra* note 10, at 295–96.

15. See DEP'T OF STATE, *supra* note 4 (discussing how Open Skies agreements seek to allow air carriers unlimited market access).

16. See Susan Carey et al., *Airlines Woo JAL to Join Global Alliances*, WALL ST. J., Sept. 18, 2009, at B1 (discussing the challenges faced by JAL after its biggest rival joined the Star Alliance).

17. See *id.* (reporting that both Delta and American Airlines offered JAL, Asia's largest volume carrier, equity stakes in order to entice JAL to join their respective alliances).

18. Warden, *supra* note 11, at 227.

19. See *id.* at 236 (discussing how excess capacity in the domestic market has been offset by Open Skies agreements).

20. *Id.* at 237.

domestic losses, the United States pressured European governments to enter into Open Skies treaties.<sup>21</sup> This, in turn, led to the formation of joint ventures and alliances between U.S. and foreign carriers who could not merge because of the ownership restrictions.<sup>22</sup> And now these joint ventures are not subject to antitrust scrutiny from the U.S. Department of Justice (DOJ) because they have received immunity from the DOT.<sup>23</sup> In sum, if the United States was not protectionist and allowed foreign investment in U.S. carriers—in other words, if they allowed the free market to operate—the airlines would not need to seek bankruptcy protection or antitrust immunity.

Even though member states of the European Union have enacted similar ownership restrictions, the United States retains an advantage because American carriers, unlike their European counterparts, can still offer service *among* European countries.<sup>24</sup> This has allowed U.S. “legacy carriers”<sup>25</sup> to maintain their dominant positions in the international travel market without fear of foreign competition.<sup>26</sup> Thus, the U.S. airlines wield considerable international market power through restrictions on foreign ownership.<sup>27</sup> Phase II of the U.S.-E.U. Open Skies Agreement is supposed to remove many of these restrictions to create a more competitive, global airline industry.<sup>28</sup>

The European Union must demand that the United States make concessions to allow increased foreign ownership of U.S. airlines. This will globalize competitive market forces in the airline industry and remove the need for immunized alliances. Further, carrier cooperation should be subject to a higher degree

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21. *Id.*

22. *Id.*

23. *Id.* Joint ventures are similar to mergers, over which the DOJ has exclusive approval authority. Reitzes & Moss, *supra* note 10, at 294–95.

24. Warden, *supra* note 11, at 236–37.

25. Terry G. Sanders, Note, *The Runway to Settlement: Rejection of Collective Bargaining Agreements in Airline Bankruptcies*, 72 BROOK. L. REV. 1401, 1403 (2007) (noting that American Airlines, United Airlines, and Continental Airlines are all such “legacy carriers”).

26. Warden, *supra* note 11, at 238.

27. *Id.* at 227, 338–39.

28. See Sharkey, *supra* note 5.

of scrutiny by the DOJ than it currently is by the DOT. Also, the United States must pass laws that create greater oversight of the DOT's power to grant antitrust immunity to alliances.<sup>29</sup> Immunity needs to be a last resort, not a first impulse. Further, the United States and European Union should attach sunset provisions to immunity grants so that alliances must regularly re-apply to maintain their privilege of immunity. This will prevent any one alliance or airline from gaining a long-term, dominant position in the global market. Without changes, all of these factors contemplate a future global airline market dominated by only three players: the three major airline alliances immune to antitrust laws.

This Comment is organized into five parts. Part II discusses the background of the airline industry and the formation of alliances, and shows how alliances affect a hypothetical passenger's itinerary from El Paso, Texas to Florence, Italy. Part III is an analysis of airline systems competition, joint venture agreements, and the immunization of alliances. Further, Part III offers an analysis of how the global "hub and spoke" airline system, predatory pricing, and collusion worries accompanying alliances undermine principles of Open Skies treaties. Part IV includes recommendations that the United States adopt former Representative Oberstar's bill limiting antitrust exemptions and that the European Union demand that the United States reduce the restrictions on foreign ownership in Phase II of the U.S.-E.U. Open Skies Treaty. Part V will conclude this Comment.

## II. FROM REGULATION TO OPEN SKIES: BACKGROUND OF THE INTERNATIONAL AIRLINE INDUSTRY

### A. *History of U.S. and European Regulation*

Since the beginning of commercial aviation, the U.S. government has heavily restricted airline competition through administrative regulation.<sup>30</sup> The Air Commerce Act of 1926

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29. See, e.g., H.R. 831, 111th Cong. (2009) (directing the Comptroller General to study antitrust exemptions).

30. See generally Christopher McBay, Comment, *Airline Deregulation Deserves Another Shot: How Foreign Investment Restrictions and Subsidies Actually Hurt the*

required U.S. citizens to own at least 51% of any registered aircraft and comprise at least two-thirds of the board of directors of any U.S. airline.<sup>31</sup> In 1938, the Civil Aeronautics Act (CAA) further restricted foreign ownership, mandating that U.S. citizens own 75% of voting rights for any U.S. carrier.<sup>32</sup> The CAA also established the Civil Aeronautics Board (CAB), which essentially established a de facto oligopoly in the airline industry. The Board was responsible for fixing prices and establishing entry barriers that protected “legacy carriers” such as American Airlines.<sup>33</sup> By 1978, the American public had grown tired of regulation, as experts testified that prices were likely 40%–100% higher due to the CAB’s price fixing.<sup>34</sup> In response, Congress passed the Airline Deregulation Act of 1978.<sup>35</sup> The benefits of deregulation were felt immediately. Within three years of deregulation there were eleven new entrants in the U.S. airline market, giving consumers lower fares, expanded routes, and more service choices.<sup>36</sup> However, the restrictions on foreign ownership remained.<sup>37</sup>

International regulation has its roots as far back as 1919 when several countries adopted the Paris Aeronautical Convention following World War I.<sup>38</sup> The core principle of the Convention was that every nation should retain sovereignty within its own airspace.<sup>39</sup> Following World War II, the major world powers convened in Chicago in order to form another, more comprehensive, multilateral agreement on aviation.<sup>40</sup> This

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*Airline Industry*, 72 J. AIR L. & COM. 173, 175–79 (2007) (discussing the history of airline regulation).

31. Christian Westra, Note, *The April 2007 U.S.-E.U. “Open Skies” Agreement: A Dream of Liberalization Deferred*, 32 B.C. INT’L & COMP. L. REV. 161, 163 (2009).

32. *Id.*

33. *See id.* (noting that the CAA did not allow a single new competitor to enter the U.S. market between 1938 and 1975); McBay, *supra* note 30, at 176–77.

34. Westra, *supra* note 31, at 163–64.

35. *Id.* at 164.

36. Robert M. Hardaway, *Of Cabbages and Cabotage: The Case for Opening up the U.S. Airline Industry to International Competition*, 34 TRANSP. L.J. 1, 4–5 (2007).

37. Westra, *supra* note 31, at 164.

38. Warden, *supra* note 11, at 229.

39. *Id.*

40. Convention on International Civil Aviation, Dec. 7, 1944, 61 Stat. 1180.

convention set the stage for U.S. dominance in the global market, as many of the United States' military planes would soon be converted to commercial use.<sup>41</sup>

Signatories to the Chicago Convention granted each other the right to fly across each other's states without landing and the right to land for non-traffic purposes.<sup>42</sup> This created the first "open" global aviation market.<sup>43</sup> While signatory states could still restrict foreign access to their airports for commercial passenger purposes, they could not deny foreign airlines access for refueling, maintenance, or emergencies.<sup>44</sup>

The United States naturally desired a more liberalized European aviation market because it already had a large fleet of planes designed specifically to fly across the Atlantic.<sup>45</sup> This desire led to Bermuda I, a significant bilateral aviation treaty between the United States and the United Kingdom.<sup>46</sup> Bermuda I called for regulation of fares and tariffs between the United States and the United Kingdom by the International Air Transport Association, with the result that the airlines competed only on capacity and service frequency, instead of price.<sup>47</sup> The new global aviation market could not shake off the U.S. system's bad habit of price regulation, and the first "airline alliance" was born.

### *B. Formation of International Airline Alliances*

Each bilateral agreement between countries technically constituted an "alliance," but while at one point it was argued that over four hundred airline alliances existed,<sup>48</sup> only three dominate today's market: (1) SkyTeam—a thirteen-carrier

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41. Warden, *supra* note 11, at 230.

42. *Id.*

43. *Id.* at 229.

44. *Id.* at 230.

45. War planes designed for WWII were subsequently sold to commercial airlines for passenger use. *Id.* at 229.

46. Westra, *supra* note 31, at 165.

47. *Id.* at 166.

48. Scott Kimpel, Comment, *Antitrust Considerations in International Airline Alliances*, 63 J. AIR L. & COM. 475, 478 (1997).

alliance dominated by Air France/KLM and Delta;<sup>49</sup> (2) Oneworld—a twelve-carrier alliance dominated by American Airlines and British Airways;<sup>50</sup> and (3) Star—a twenty-seven-carrier alliance dominated by three American carriers (Continental, United, and U.S. Airways) and Lufthansa.<sup>51</sup>

Modern international airline alliances first began with the formation of the Northwest/KLM alliance (informally referred to as “Wings” throughout the airline industry) in 1993, when it received antitrust immunity from the DOT.<sup>52</sup> The purpose behind the formation of alliances was to circumvent foreign ownership restrictions of national airlines.<sup>53</sup> For example, in order for an airline to carry domestic traffic in the United States (i.e., to fly from New York to Los Angeles) the airline carrier must be a U.S. citizen.<sup>54</sup> A U.S. citizen airline is an airline that (1) has U.S. citizens as two-thirds of its board and (2) has at least 75% of the voting interest owned by U.S. citizens.<sup>55</sup> In other words, British Airways cannot service the New York-Los Angeles route mentioned above, and if Air France were to merge with a U.S. carrier, such as American Airlines, the new AA/Air France carrier could no longer serve the New York-Los Angeles

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49. *Our Carriers*, SKYTEAM, <http://www.skyteam.com/about/carriers/index.html> (last visited Feb. 26, 2011) [hereinafter SKYTEAM].

50. *Member Airlines*, ONEWORLD, <http://www.oneworld.com/ow/member-airlines/> (last visited Feb. 26, 2011) [hereinafter ONEWORLD].

51. *Member Airlines*, STAR ALLIANCE, <http://www.staralliance.com/en/about/airlines/> (last visited Feb. 26, 2011) [hereinafter STAR ALLIANCE].

52. Charles N.W. Schlangen, Comment, *Differing Views of Competition: Antitrust Review of International Airline Alliances*, 2000 U. CHI. LEGAL F. 413, 415 (2000). Ironically, Northwest and KLM undertook the 1993 venture in order to stave off bankruptcy filings. See Shawn Tully & Therese Eiben, *The Alliance From Hell*, FORTUNE, June 24, 1996, at 64. Subsequently, Northwest Airlines filed for bankruptcy and eventually merged with Delta Airlines, while KLM merged with Air France. *Delta, Northwest Approve Merger Deal*, CBS NEWS (Apr. 14, 2008), <http://www.cbsnews.com/stories/2008/04/14/business/main4014360.shtml>; *Air France and KLM Get Close*, ECONOMIST, Oct. 6, 2003, available at <http://www.economist.com/node/2098740>. Both are now members, again, of the same alliance: SkyTeam. SKYTEAM, *supra* note 49.

53. See Schlangen, *supra* note 52, at 416.

54. *Id.*

55. See 49 U.S.C. § 40102(a)(15)(C) (2006).

market either. Naturally though, both American Airlines and British Airways want to offer international service to their customers; hence, the formation of an alliance.

Even with some anticompetitive concerns, alliances do create many benefits for consumers. Alliances allow member carriers to integrate their ticketing and baggage handling procedures.<sup>56</sup> To the international traveler, it “feels” like he or she booked a ticket on one airline because the traveler’s bags and tickets are automatically transferred between alliance members. The code-sharing aspect of the alliance creates efficiencies for the airlines, conveniences for the passengers, and, to some extent, loyalty to a particular alliance.<sup>57</sup> Below is an example of how a typical international passenger can benefit from flying on an alliance carrier.

### C. Hypothetical Passenger Example

A passenger flying from El Paso, Texas to Florence, Italy could not fly direct or use the same carrier throughout the journey.<sup>58</sup> Instead, the passenger would first have to travel to a major U.S. hub, such as Houston, on a U.S. citizen airline because the El Paso-Houston route is domestic only. Second, the passenger would then have to fly to a European hub from the U.S. hub in order to catch a connecting flight to Florence. This is called gateway-to-gateway traffic, consisting of flights from major U.S. hubs to major European hubs (i.e., New York-London, Houston-Paris, etc.).<sup>59</sup> Last, the passenger would fly from the European hub to his final destination of Florence, Italy. It is likely that this last leg of the journey would have to be on a European carrier because most countries have foreign ownership restrictions.<sup>60</sup>

The hypothetical passenger’s final itinerary would look something like this: (1) El Paso-Houston, (2) Houston-Paris, (3)

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56. Daniel Hedlund, Note, *Toward Open Skies: Liberalizing Trade in International Airline Service*, 3 MINN. J. GLOBAL TRADE 259, 273 (1994).

57. Reitzes & Moss, *supra* note 10, at 299.

58. As discussed earlier, this is due to the United States’ foreign ownership restrictions on airlines. See *supra* Part II.A–B.

59. See Reitzes & Moss, *supra* note 10, at 297–98.

60. See Schlangen, *supra* note 52, at 416.

Paris-Florence. If the passenger used airlines that were members of the same alliance, such as Continental and Air France, he could utilize the benefits of the two airlines' code-sharing agreement.

If the hypothetical passenger used Continental Airlines to fly from El Paso to Houston (Continental's North American hub),<sup>61</sup> Air France from Houston to Paris, and Air France again from Paris to Florence. Because Continental and Air France are members of the same alliance, it would be as though the passenger had booked the entire trip with one airline. The passenger's baggage would be automatically checked through to the final destination, the passenger would only have to check in one time, and the passenger would receive frequent-flier miles for the whole trip.<sup>62</sup> Code-sharing also enables airline partners to offer their customers more service options.<sup>63</sup> Customers are able to book flights to any world destination served by their alliance and utilize alliance airport lounges.<sup>64</sup>

The above hypothetical passenger's journey is a product of international airline alliances and systems competition. Due to foreign ownership restrictions and competitive behavior in domestic markets, the U.S. airline industry has formed into a "hub-and-spoke" system with each major airline dominating a certain city's hub and offering service to destinations throughout the country.<sup>65</sup> This hub-and-spoke model has been copied into the international market.<sup>66</sup>

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61. See *Continental Reopens Terminal C, Plans Service from IAH to New Zealand*, HOUS. BUS. J., May 26, 2010, available at <http://www.bizjournals.com/houston/stories/2010/05/24/daily30.html>.

62. Schlangen, *supra* note 52, at 416–17.

63. *Id.* at 417.

64. *Id.*

65. See Hedlund, *supra* note 56, at 282.

66. András Farkas et al., *Europe's Best Airline Network Managers May Have Won an Unassailable Lead*, MCKINSEY Q., 1997 no. 3, at 180.

### III. SYSTEMS COMPETITION: ALLIANCE SYSTEMS AND OPEN SKIES

The transatlantic aviation market can be divided into four markets based upon a passenger's origin and destination point:<sup>67</sup>

- (1) Gateway-to-Gateway: This market encompasses travelers that begin and end their trips at U.S. and European airline hubs (e.g., New York-London or Houston-Paris).<sup>68</sup>
- (2) Behind-Gateway-to-Gateway: This market encompasses travelers that must first take a domestic flight to reach a major U.S. gateway (e.g., a passenger flying from El Paso to Paris: (a) El Paso-Houston; (b) Houston-Paris).<sup>69</sup>
- (3) Gateway-to-Beyond-Gateway: This market encompasses travelers from major U.S. hubs that must catch a connecting flight in a European hub to reach their final destination (e.g., a passenger flying from Houston to Florence: (a) Houston-Paris; (b) Paris-Florence).<sup>70</sup>
- (4) Behind-Gateway-to-Beyond-Gateway: This market encompasses travelers like the hypothetical posed in Part II.C (e.g., a passenger flying from El Paso to Florence: (a) El Paso-Houston; (b) Houston-Paris; (c) Paris-Florence).<sup>71</sup>

Dividing the transatlantic aviation market into these four sub-markets provides a convenient framework for analyzing a hub-dominated structure based on network effects (sometimes referred to as a "star" network).<sup>72</sup> The term "network effects" describes a system where the value to any given user increases

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67. Reitzes & Moss, *supra* note 10, at 318 (summarizing market surveys and data collection made by the DOT in a 1999 study).

68. *Id.*

69. *Id.*

70. *Id.*

71. *Id.*

72. *See id.* at 298, 318.

as each additional user joins the system.<sup>73</sup> The typical example of this is the word processor. The more people that use Microsoft Word, the more valuable the program is to the user because she can interchange files, edit, e-mail, and share documents with her coworkers using only a single system.<sup>74</sup> In sum, the more people that use the same word processor, the more valuable the word processor software becomes to its user.

Similarly, every time an airline adds service to a new location, customers at that new location now have access to that airline's hub, and thus access to anywhere that airline flies.<sup>75</sup> This effect is expanded with respect to international alliances, as each added carrier brings a host of new destinations to that alliance system. This also adds utility to customers already in the alliance who now have access to a new location.<sup>76</sup>

However, this system also creates some potential anticompetitive effects because, due to its design, passengers *must* fly through one of these hubs, which creates inefficiencies and problems concerning market allocation.<sup>77</sup> For example, refer back to the hypothetical passenger flying from El Paso to Florence. The most efficient itinerary for this hypothetical passenger is likely already determined for him by an alliance. Alternatively, his route will be determined by a number of factors used by the customer in choosing his ticket, such as:

- (1) Time Sensitivity - When does the passenger need to be there? Business passengers tend to book on short notice, prefer shorter flight times, less layovers, and typically occupy first or business class seats.<sup>78</sup>
- (2) Cost - Prices of the tickets will have great influence on

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73. Max Schanzbach, *Network Effects and Antitrust Law: Predation, Affirmative Defenses, and the Case of U.S. v. Microsoft*, 2002 STAN. TECH. L. REV. 4, 6–9 (2002).

74. *See id.*

75. Reitzes & Moss, *supra* note 10, at 299.

76. *See id.*

77. *See contra* Michael E. Levine, *Airline Alliances and Systems Competition: Antitrust Policy Toward Airlines and the Department of Justice Guidelines*, 45 HOUS. L. REV. 333 (2008) (arguing the network benefits of hub carrier competition and how non-network independent carriers discipline the market sufficiently to mitigate any anticompetitive effects).

78. *See* Martijn Brons et al., *Price Elasticities of Demand for Passenger Air Travel: A Meta-Analysis*, 8 J. AIR TRANSP. MGMT. 165, 168 (2002).

the leisure traveler.<sup>79</sup>

- (3) Alliance/Airline Preference - Some customers prefer airlines based on quality of service, and with the advent of frequent flier miles, brand loyalty has become a major factor in customer preferences.<sup>80</sup>

First, an examination of the “hub-and-spoke” system of airline competition reveals that the hypothetical passenger may not even have a choice in carrier. This is primarily due to the large carriers’ ability to drive low cost carriers from the market.<sup>81</sup> In alliance systems, this happens because alliance partners engage in conduct that makes it unprofitable for non-alliance members to access their “hub” market.<sup>82</sup>

The dominant hub carrier charges interlining fees to airlines carrying passengers that are connecting to a flight on the dominant carrier.<sup>83</sup> For example, dominant hub airline, Airline X, charges fees to all non-alliance carriers that have to connect in its hub airport. By raising these fees, fewer passengers will choose non-alliance carrier, Carrier Y, to connect to a flight at Airline X’s hub. Airline X would also want to do this because most alliances are revenue-sharing. Thus, Airline X makes money off of every connecting passenger brought to its airport by an alliance member. This type of agreement is commonly called a joint venture.<sup>84</sup>

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79. *See id.* at 167. A search for economy airline tickets from El Paso, TX to Florence, Italy one month in advance revealed that flights with shorter flight times were generally more expensive; for example, one flight option with duration of approximately twenty-three hours cost \$799, while another option with duration of approximately fifteen hours cost \$942. Flight Search Results from El Paso, TX to Florence, Italy, CONTINENTAL AIRLINES, <http://www.continental.com> (follow “Make Flight Reservation” hyperlink, then search for economy flights from El Paso, TX to Florence, Italy departing Mar. 3, 2011 and returning Mar. 9, 2011).

80. *See* Paul Stephen Dempsey, *The Financial Performance of the Airline Industry Post-Deregulation*, 45 HOUS. L. REV. 421, 453–55 (2008).

81. *See id.* at 471 (arguing that large carriers often cut prices and increase capacity in order to edge new competitors out of the market and maintain dominance in the threatened routes).

82. *See* Reitzes & Moss, *supra* note 10, at 309–11.

83. *See id.* at 306 n.47.

84. *See* Kimpel, *supra* note 48, at 476–77.

### A. Airline Joint Ventures

Among airline alliances, a joint venture's goal is to promote "metal neutrality", a commercial environment in which joint venture partners share common economic incentives to promote the success of the alliance over their individual corporate interests."<sup>85</sup> Through joint pricing and revenue sharing, the airlines are able to cooperate and coordinate their pricing and scheduling and hence are supposedly "able to focus on gaining the customer's business by providing the best available fare and routing between two cities."<sup>86</sup>

This principle is best illustrated by returning to the previous example.<sup>87</sup> Suppose Continental, Delta, and Air France are all in the same airline alliance.<sup>88</sup> Continental and Delta are supposed to compete for service on the "behind-gateway" portion of the passenger's journey.<sup>89</sup> However, all three airlines are indifferent as to which carrier actually took the passenger across the Atlantic to Paris, as they all share equally in the revenue from that ticket.

By contrast, once the passenger gets to Paris, Air France has a strong incentive to make sure that he takes an Air France connecting flight to his final destination of Florence. Once the passenger is in Europe, Air France must compete with the other European carriers for his connecting flight to Florence, and Air

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85. Show Cause Order to Amend Order 2007-2-16 so as to Approve and Confer Antitrust Immunity, Docket DOT-OST-2008-0234, order: 2009-4-5 at 4 (Dep't of Transp. Apr. 7, 2009) [hereinafter Show Cause Order]. Sometimes this principle is also referred to as "sales without preference." Final Order to Amend Order 2007-2-16 so as to Approve and Confer Antitrust Immunity, Docket DOT-OST-2008-0234, order: 2009-7-10 at 24 (Dep't of Transp. July 10, 2009) [hereinafter A++ Final Order].

86. Show Cause Order, *supra* note 85, at 3-4.

87. See *supra* text accompanying note 61 (discussing the El Paso-Florence route example).

88. These were the major airlines of the SkyTeam Alliance before the Continental switch. See Press Release, SkyTeam (Dec. 2004), available at <http://www.skyteam.com/news/headlines/20041217.html>.

89. The "behind-gateway" portion of the journey in the hypothetical is the route between El Paso and another U.S. hub. Reitzes & Moss, *supra* note 10, at 298 (explaining that destinations "behind the gateway" are smaller cities that are not major hubs).

France does *not* have to share revenues from this trip. However, if Air France's alliance can get the passenger to book his first behind-gateway flight on a fellow alliance carrier, then Air France could recoup any lost revenue on the connecting flight due to the benefits of the shared alliance revenue.

Perhaps the best way to think about a joint venture is as "an alliance within an alliance."<sup>90</sup> A select few carriers of a larger alliance agree to integrate and cooperate in order to achieve metal neutrality.<sup>91</sup> Generally, airline joint ventures greatly enhance the airline alliance's ability to pool resources, operate efficiently, offer more travel options, and pass savings on to consumers.<sup>92</sup> This is accomplished through a variety of methods, including code sharing, frequent-flyer reciprocity, and through-ticketing.<sup>93</sup> However, without immunity, the carriers would still be subject to the antitrust laws of the United States and European Union, and therefore could not engage in joint pricing or revenue sharing without probable antitrust scrutiny from the Department of Justice.<sup>94</sup>

#### *B. DOT Grant of Antitrust Immunity*

Before the Department of Transportation will grant antitrust immunity to applicant carriers wishing to create a joint venture or alliance, the DOT requires an Open Skies agreement to be in place between the United States and all the foreign carriers' native countries.<sup>95</sup> The applicants then submit all data and documents necessary to prove that their alliance is in the public interest and that the grant of immunity will produce public benefits not otherwise available without antitrust immunity.<sup>96</sup> Further, the applicants must show that their cooperative agreement will not substantially reduce

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90. See John Burton & Pat Hanlon, *Airline Alliances: Cooperating to Compete?*, 1 J. AIR TRANSP. MGMT. 209, 225 (1994).

91. Show Cause Order, *supra* note 85, at 4.

92. Comments of the Dep't of Justice on the Show Cause Order, Docket DOT-OST-2008-0234 at 29–30 (Dep't of Transp., June 26, 2009) [hereinafter DOJ Comments].

93. *Id.* at 30.

94. *Id.* at 6–7.

95. Show Cause Order, *supra* note 85, at 2.

96. See *id.* at 1–4.

competition.<sup>97</sup> However, it is unclear whether the DOT takes a more lenient approach to what conduct constitutes “substantial reduction of competition” in this context than the DOJ does under the Sherman Act.<sup>98</sup>

After the DOT has concluded its initial investigation, it makes a tentative decision.<sup>99</sup> It then asks for all interested parties to “show cause” why it should not make its tentative findings final, and accepts submissions from parties over the next twenty-one calendar days.<sup>100</sup> The DOT considers the submissions, notably the comments from the DOJ and other federal agencies, and adjusts its findings as needed.<sup>101</sup>

Common compromises between the DOJ and DOT in these proceedings are “carve outs,” which effectively withhold immunity from a few key transatlantic routes.<sup>102</sup> Typically, if the proposed alliance involves carriers with key overlapping routes, the DOT will disallow cooperation on those routes to maintain a competitive structure.<sup>103</sup> These city-pairs often involve competitor carriers that offer nonstop service between the two cities, where the effects of reduced competition would be imparted on “time sensitive travelers” such as businesspersons.<sup>104</sup>

After determining the need for any carve outs, and barring any substantial new evidence, the DOT confirms its initial order to grant or deny antitrust immunity.<sup>105</sup> Typically, the order contains conditions, exceptions, limitations, and other provisions

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97. *Id.* at 1.

98. *See id.* at 14 (noting that the DOT balances the benefits of the alliance with the risks of consumer harm, which differs from the DOJ’s analysis in the Continental application to join Star).

99. *See* A++ Final Order, *supra* note 85, at 3–4.

100. *See* Show Cause Order, *supra* note 85, at 26.

101. *See* A++ Final Order, *supra* note 85, at 5–6.

102. *See id.* at 18.

103. *See id.* For example, in the Continental-Star ATI Application, the DOT made four city-pair carve outs in its decision to grant immunity. *Id.* They were (a) Washington-Frankfurt, (b) Chicago-Frankfurt, (c) San Francisco-Toronto, and (d) Chicago-Toronto. *Id.* at 18 n.74. The purpose of the carve outs on these city pairs was to prevent the joint venture from reducing nonstop competitors from two to one. *Id.*

104. *Id.*

105. *See* A++ Final Order, *supra* note 85, at 1–2.

that alter the scope of immunity, sometimes including grants of special privileges to a joint venture within the alliance.<sup>106</sup>

*C. The Atlantic-Plus-Plus Agreement (A++) and the Continental-Star ATI Agreement*<sup>107</sup>

Within the Star Alliance, United Airlines, Air Canada, and Lufthansa created a joint venture agreement called Star ATI to enable greater integration of the airlines on transatlantic routes.<sup>108</sup> The carriers instituted revenue sharing on transatlantic routes in 2003 and labeled the venture the Atlantic Plus (A+) Agreement.<sup>109</sup> This venture was approved by the DOT, which granted the participants in A+ “global antitrust immunity” within the United States.<sup>110</sup> In its 2008 application to the DOT, Continental Airlines, along with the other Star ATI members, requested to form a new joint venture, labeled Atlantic-Plus-Plus (A++), which would allow Continental to switch from the unimmunized SkyTeam joint venture to join Star with antitrust immunity.<sup>111</sup>

Continental and the other carriers of Star ATI (Applicants), argued that approval of A++ with antitrust immunity was required due to “highly adverse industry conditions.”<sup>112</sup> The Applicants argued that the “[e]xtreme and unprecedented increases in the price of jet fuel, combined with the slowdown in

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106. A++ Final Order, *supra* note 85, at app. A.

107. In all documents filed with the DOT and made available to the public, the contents of the A++ Joint Venture have been redacted and made confidential in accordance with 14 C.F.R. § 302.12. FTC Objections to Public Disclosure of Information, 14 C.F.R. § 302.12 (2010). *See generally* A++ Final Order, *supra* note 85.

108. Final Order on Joint Application for Approval of and Antitrust Immunity for Commercial Alliance Agreements, Docket OST-96-1434, order 2007-2-16 at 3 (Dep’t of Transp. Feb. 13, 2007) [hereinafter Atlantic Plus (A+) Final Order]. Other participants in the agreement include Swiss Airlines, Air Portugal, and British Midland Airways. *Id.* at 4–5.

109. DOJ Comments, *supra* note 92, at 5.

110. *Id.*

111. Joint Application of Continental Airlines et al. to Amend Order 2007-2-16 so as to Approve and Confer Antitrust Immunity on Certain Alliance Agreements, Docket DOT-OST-2008-0234, at 3–4 (Star Alliance, July 23, 2008) [hereinafter Joint Application].

112. *Id.* at 4.

the U.S. and wider global economy, have created a crisis for U.S. airlines.”<sup>113</sup> In order to combat higher jet fuel prices, the Applicants argued that the addition of Continental would complement the alliance’s route network and allow them to “coordinate the services they operate on transatlantic routes.”<sup>114</sup> In combination with higher fuel prices, the general economic climate of the airline industry has been consistently deteriorating since 9/11.<sup>115</sup> Some of the factors contributing to the poor economic condition of airlines include the inability to secure loans<sup>116</sup> and overcapacity by the airlines on certain routes.<sup>117</sup>

Further, the Applicants argued that DOT’s grant of immunity was necessary to compete with the immunized and “more deeply integrated SkyTeam Alliance,” which now includes Delta/Northwest.<sup>118</sup> Continental and the other applicants repeatedly asserted that the main motivation behind Continental’s switch and application for antitrust immunity was to respond to the merger between Delta and Northwest.<sup>119</sup> Following the Delta/Northwest merger, a group of SkyTeam carriers formed a joint venture, of which Continental was not a

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113. *Id.* at 4–5.

114. *Id.* at 6.

115. See Kristina McQuaid, Comment, *Delta & Northwest File for Bankruptcy: Is it Time to Ground a Major Airline?*, 29 HOUS. J. INT’L L. 663, 664–67 (2007) (noting several factors contributing to the poor economic condition of the airline industry).

116. *Id.* at 667. Most carriers’ assets are already pledged collateral, and the airlines’ revenue is more dependent on leisure travel than in years past. *Id.* Also, leisure passengers are booking more tickets online, allowing them to compare prices more readily and wait for the best price. *Id.* at 668. Further, leisure customers are increasingly purchasing online airfare from third party websites that utilize algorithms that can tell the consumer the best time to buy for the lowest price. See, e.g., *Bing Travel*, BING, <http://www.bing.com/travel/?cid=homenav&FORM=Z9LH5> (last visited Feb. 25, 2011).

117. McQuaid, *supra* note 115, at 668 (noting that “profit has declined due to excess numbers of available seats”).

118. Joint Application, *supra* note 111, at 5. The Applicants argued that rising fuel prices were a major factor contributing to DOT’s approval of the Delta/Northwest merger, and thus should also apply to the Applicants’ request for antitrust immunity. *Id.* at 4–5.

119. See, e.g., Larry Kellner, Chairman & CEO, Continental Airlines, *Star Alliance-Continental Induction Ceremony*, YOUTUBE (Oct. 28, 2009), [http://www.youtube.com/watch?v=w\\_o3MMTe97A&feature=related](http://www.youtube.com/watch?v=w_o3MMTe97A&feature=related).

party, and received approval and antitrust immunity from the DOT.<sup>120</sup> Likely, Continental had the feeling that it was being “pushed out” of the SkyTeam international market, since it could not share in the revenues generated by the joint venture between Delta/Northwest and Air France/KLM on transatlantic routes.<sup>121</sup>

While there has been an increase in jet fuel prices over the last five years or so, the peak oil prices occurred around the same time that the Applicants filed for immunity.<sup>122</sup> Since the summer of 2008, jet fuel prices have dropped dramatically and have now somewhat leveled off.<sup>123</sup> When Continental and Star submitted their application, the price of jet fuel was peaking around \$170-\$180/barrel.<sup>124</sup> However, since the summer of 2008, jet fuel prices dropped to as low as \$50/barrel in May 2009 and leveled off around \$80/barrel in January 2010.<sup>125</sup> Thus, since Continental’s application was a “direct response to the unprecedented fuel crisis,”<sup>126</sup> and such fuel crisis had since passed, it is unclear why the DOT relied so heavily on rising fuel prices in granting the Applicants global antitrust immunity.<sup>127</sup>

In addition, the DOT has authority to grant antitrust immunity only when it is required by the public interest and when the applicant would not otherwise go forward with the transaction.<sup>128</sup> The statutory framework for antitrust immunity can be translated thus: the applicant must show that the agreement will produce significant public benefits and that the applicant will not go forward with the agreement without antitrust immunity.<sup>129</sup>

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120. Joint Application, *supra* note 111, at 7.

121. *See id.* at 7–8.

122. *Id.* at 1, 7–8. *See Analysis of Jet Fuel Prices*, INT’L AIR TRANSP. ASS’N, [http://www.iata.org/whatwedo/economics/fuel\\_monitor/Pages/price\\_analysis.aspx](http://www.iata.org/whatwedo/economics/fuel_monitor/Pages/price_analysis.aspx) (last visited Feb. 26, 2011).

123. *Analysis of Jet Fuel Prices*, *supra* note 122.

124. *Id.*

125. *Id.*

126. Joint Application, *supra* note 111, at 4.

127. A++ Final Order, *supra* note 85, at 26.

128. 49 U.S.C. § 41308 (2010).

129. *See DOJ Comments*, *supra* note 92, at 12.

The Star Alliance applicants assured the DOT that immunity for A++ would allow them to more effectively compete with the immunized SkyTeam joint venture.<sup>130</sup> However, it has been longstanding U.S. policy that the antitrust laws are “concern[ed] with the protection of competition, not competitors.”<sup>131</sup> Thus, just because antitrust immunity may allow the carriers of Star to better compete with SkyTeam and Oneworld on transatlantic routes, that rationale alone does not justify approval. There must be significant *consumer benefits*, in the form of lower prices or expanded service options, such that the agreement is “required by the public interest.”<sup>132</sup> Granting antitrust immunity to Star members so that they can better compete with other carriers is simply not justifiable under the statute.

Similarly, the Star Applicants relied on the DOT’s recent decision to grant the SkyTeam joint venture antitrust immunity as support for their application.<sup>133</sup> This argument, which compares apples to oranges, is futile. Delta and Northwest both filed for bankruptcy in 2007 and were on the verge of receiving bankruptcy protection from their creditors when their shareholders approved their merger.<sup>134</sup> The applicants of the Star ATI agreement were not in a comparable financial crisis at the time of their application.<sup>135</sup> Further, at the time the Star ATI applicants submitted their application, the American/British Airways Oneworld Alliance did not operate its transatlantic joint venture with antitrust immunity, as it was

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130. Joint Application, *supra* note 111, at 2.

131. *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962).

132. 49 U.S.C. § 41308.

133. See Final Order on Joint Application of Alitalia-Linee Aeree Italiane-S.P.A. et al., for Approval of and Antitrust Immunity for Alliance Agreements, Docket OST-2007-28644-0185, Order: 2008-5-32 at 2 (Dep’t of Transp. July 10, 2009) (granting antitrust immunity to a joint venture between Delta/Northwest and Air France/KLM).

134. See DELTA AIRLINES, INC. & NORTHWEST AIRLINES CORP., AGREEMENT AND PLAN OF MERGER 9, 29 (2008).

135. Darren Shannon, *Justice Slams DOT Star ATI Approval*, AVIATION WEEK (June 29, 2009), [http://www.aviationweek.com/aw/generic/story\\_channel.jsp?channel=comm&id=news/STAR06299.xml](http://www.aviationweek.com/aw/generic/story_channel.jsp?channel=comm&id=news/STAR06299.xml).

denied immunity by the DOT in 2002.<sup>136</sup>

However, once the DOT had conferred immunity on both Star and SkyTeam, it became much more likely that Oneworld, the only remaining major alliance without transatlantic joint venture immunity, could successfully reapply for immunity. In this respect, the argument that “I should get it because you gave it to them” threatens to snowball into a scenario where, having granted all three major alliances antitrust immunity, the DOT and the DOJ will be unable to effectively enforce competition between them.

While the Star ATI Applicants argued that immunity was necessary in order to effectuate the A++ agreement’s provision on revenue sharing, they did not sufficiently explain why they could not achieve the desired benefits without immunity.<sup>137</sup> Most of the quantitative data regarding consumer benefits, such as pricing and route scheduling fares, is kept confidential from the public.<sup>138</sup> However, according to the DOJ, the Applicants did not present any evidence that customers would “receive quantitatively or qualitatively different service” if Continental merely operated at a level of cooperation that did not require antitrust immunity.<sup>139</sup>

#### *D. Immune Alliances Undermine Open Skies Agreements*

The U.S.-E.U. Air Transport Agreement, commonly known as “Open Skies” was signed April 30, 2007, and took effect on March 20, 2008.<sup>140</sup> At its heart, the Open Skies Agreement wipes away the old model of regulation by individual countries and “opens up the skies” to foreign airlines.<sup>141</sup> Under the old

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136. *Oneworld Leaders Vow to Continue Alliance*, FT. WORTH STAR-TELEGRAM, Feb. 22, 2002, at BU2. *See also* Karp, *supra* note 13 (noting that Oneworld was nevertheless granted antitrust immunity in 2010).

137. The airlines would have to receive antitrust immunity in order to share the pricing and other sensitive information needed to effectively share the revenues of the transatlantic routes. Joint Application, *supra* note 111, at 12.

138. Harvey A. Strickon, *Can Antitrust Violations in the Aircraft Industry Truly Exist?*, 20 AIR & SPACE LAW. 14, 15 (2006).

139. DOJ Comments, *supra* note 92, at 30.

140. U.S.-E.U. Open Skies, *supra* note 3.

141. *See* Westra, *supra* note 31, at 162–67.

international regulation model, each country was free to place whatever restrictions they desired on aviation coming into its skies and airports.<sup>142</sup> Notably, this included restricting: a) which cities/airports foreign carriers were allowed to fly to; b) when foreign carriers were allowed to land and take off (often only at inconvenient times); c) how many flights the carrier was allowed to bring in; (d) the size and/or type of aircraft the foreign carrier was allowed to fly; and (e) how many gates the carrier was allowed to use at the airport.<sup>143</sup>

Naturally, this allowed countries to favor native airlines over foreign ones.<sup>144</sup> Thus, one of the key provisions of the Open Skies Agreement is a “grant of rights” that permits each U.S. or E.U. airline to fly freely from any city in the United States to any city in the European Union and vice versa.<sup>145</sup> Further, the agreement provides that no country “shall unilaterally limit the volume of traffic, frequency or regularity of service, or the aircraft type or types operated” by a foreign airline.<sup>146</sup>

While it seems that almost all of the “old international regulations” have been swept away, the agreement does prohibit foreign carriers from participating in or competing in purely domestic service.<sup>147</sup> For example, Air France cannot service a route from New York to Los Angeles, just as Continental Airlines could not service a flight from Paris to Rome. Also, the agreement restricts foreign ownership of native airlines.<sup>148</sup> For example, non-U.S. citizens or corporations cannot own more than a 25% voting equity in Continental Airlines, nor control the airline outright by owning more than a 50% total equity in the

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142. *See id.* at 162–66.

143. *See id.*

144. For example, the United Kingdom would ensure that British Airways had the most international traffic and control of more than enough international gates at London’s Heathrow Airport. *See* Press Release, U.S. Embassy—Belgium, U.S. E.U. Reach Long-Sought Accord To Liberalize Air Traffic (Mar. 2, 2007), *available at* <http://www.america.gov/st/washfile-english/2007/March/20070302164135saikceinawz0.3534967.html>.

145. U.S.-E.U. Open Skies, *supra* note 3, at art. 3(1)(c).

146. *Id.* at art. 3(4).

147. *Id.* at art. 3(6).

148. *Id.* at annex 4 art. 1(1).

company.<sup>149</sup>

It is the stated policy of the DOT that a condition for receiving antitrust immunity for a proposed joint venture is that there must first be an Open Skies agreement in place with all host countries.<sup>150</sup> Necessarily, this must be considered a good thing. The Open Skies agreements greatly liberalized the international aviation markets and greatly enhanced global competition.<sup>151</sup> In other words, under the old regulatory scheme, consumers likely only had one choice to fly to Paris: Air France. Now however, consumers have many choices of airlines, times, flight schedules, and prices.

Because of the great consumer benefits and enhanced competition created by Open Skies agreements, the United States made an effort to negotiate and enter into as many Open Skies agreements with as many countries as possible.<sup>152</sup> This opened up foreign national markets to U.S. airlines, particularly the “legacy carriers” who dominate international travel (American, United, Delta, etc.).<sup>153</sup> These newly established international routes were highly lucrative for U.S. air carriers.<sup>154</sup>

As the world undergoes a transformation into a more truly global economy there has been a rise in both global business and leisure travelers.<sup>155</sup> Thus, the world’s largest airlines started forming airline alliances to coordinate the rising global needs of passengers.<sup>156</sup> As the world’s airlines began joining the three main alliances, the U.S. DOT also began granting them immunity from the U.S. antitrust laws.<sup>157</sup> Many of these grants

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149. *Id.* These restrictions are mandated by Congress under a theory of national security. *See Westra, supra* note 31, at 170–71. While negotiating the Open Skies Agreement, the United States made its signing of the treaty with the European Union contingent on the inclusion of this provision. *See id.* at 169–71.

150. A++ Final Order, *supra* note 85, at 11.

151. *Id.*

152. DOJ Comments, *supra* note 92, at 13–14.

153. *See id.* at 14.

154. *See Westra, supra* note 31, at 173–74.

155. *See McQuaid, supra* note 115, at 694.

156. *See supra* Part II.B.

157. DOJ Comments, *supra* note 92, at 13.

were intended to “further the foreign policy goal of inducing the governments of the foreign alliance partners’ home countries to enter into [O]pen [S]kies agreements with the United States.”<sup>158</sup>

Indeed, the idea of “open skies” and increased competition is directly opposite to the idea of antitrust immunity, or immunity from laws that further a competitive market. The DOT recognized such in its approval of the original Northwest/KLM alliance, but concluded that “[i]n this case, however, the grant of immunity should promote competition by furthering our efforts to obtain less restrictive aviation agreements with other European countries.”<sup>159</sup>

The problem with the DOT’s grant of immunity to the Continental-Star ATI joint venture is that the United States already has secured an Open Skies agreement with the member states of the E.U.<sup>160</sup> It is questionable then exactly how Continental’s immunity furthers U.S. foreign air transportation policy; it would seem that it merely benefits the four airlines of the A++ joint venture, two of which, United and Continental, are American-based.<sup>161</sup>

The DOT argues that its decision to grant antitrust immunity to the Star ATI joint venture was carefully considered and will benefit both U.S. and E.U. foreign policy goals.<sup>162</sup> Mainly, however, the DOT appears to be concerned about its own credibility.<sup>163</sup> It believes that the European Union and other countries may see a denial of antitrust immunity to Star ATI as a failure of the United States to hold up its part of the bargain in the Open Skies Agreement.<sup>164</sup>

However, two things undermine this argument. First, the plain meaning of the U.S.-E.U. Open Skies Agreement gives the

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158. *Id.* at 13–14.

159. *Id.* at 14 (internal quotes omitted).

160. *Id.* Though the United States and the European Union have agreed to Phase II of the U.S.-E.U. Open Skies Agreement there is “no claim . . . that granting expanded immunity to Star would lead to success in those negotiations.” *Id.* at 14 n.40.

161. See A++ Final Order, *supra* note 85, at 1. The other two airlines are Air Canada and Lufthansa. *Id.*

162. *Id.* at 11.

163. *Id.*

164. *Id.*

DOT independent review of antitrust concerns with cooperative agreements among airline carriers.<sup>165</sup> The agreement does so by excluding all “competition disputes” from binding arbitration between the two disputing parties.<sup>166</sup> Antitrust and competition disputes are to be resolved by the DOT or the European Commission, respectively.<sup>167</sup> All other disputes under the agreement must be resolved by arbitration.<sup>168</sup>

Second, the agreement provides that the DOT and the European Commission are to cooperate in order to be more “consistent with their respective functions in addressing competition issues.”<sup>169</sup> The treaty goes on to say that the two regulatory entities are to share competition experts’ reports and jointly evaluate competition in the transatlantic market.<sup>170</sup> However, as soon as the DOT approved antitrust immunity for the Star ATI alliance, the European Commission announced that it was continuing its investigation of the proposed cooperation of the four Star Alliance airlines.<sup>171</sup>

The DOT apparently granted Star ATI antitrust immunity without the goal of inducing other Open Skies agreements with other countries, and without the cooperation of the European Commission. This pattern of recklessly granting immunity to applicants could be disastrous for consumers.

In the last sixteen years, the United States has formed Open Skies agreements with ninety-four countries, and the DOT has granted antitrust immunity to more than twenty alliance

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165. U.S.-E.U. Open Skies, *supra* note 3, at annex 2 art. 1.

166. *Id.* at art. 19, 20.

167. *Id.* at annex 2 art. 1.

168. *Id.* at art. 19(1).

169. *Id.* at annex 2 art. 1.

170. *Id.* at annex 2 art. 4.

171. Press Release, European Comm’n, Commission Confirms Sending Statement of Objections to Three Members of Oneworld Alliance, (Oct. 2, 2009), *available at* <http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/09/430&format=HTML&aged=0&language=EN&guiLanguage=en> (announcing that the Commission intended to continue its “parallel investigations” into Star). The DOT’s Final Order granting antitrust immunity was released July 10, 2009, three months before the European Commission’s press release. *See* A++ Final Order, *supra* note 85, at 1.

agreements.<sup>172</sup> These numbers are indicative of the large extent to which the international airline industry has rapidly become deregulated.<sup>173</sup> While deregulation is good for competition and allows market forces to set important items like price, capacity, and scheduling, basic principles of antitrust law should still be a concern with international airline alliances. If basic theories of economics and antitrust policy are ignored, consumers will likely end up with a transatlantic aviation system comprised of three dominant players—the alliances—that are all immune from the world's antitrust laws.

*E. The Global Hub and Spoke Model*

As discussed previously, the transatlantic airline alliance market has created a hub-and-spoke model of systems competition.<sup>174</sup> This system results in increased traffic density on gateway-to-gateway routes, such as New York to London.<sup>175</sup> This system of competition probably naturally formed after deregulation because it creates “significant cost economies resulting from increased traffic density, particularly as they induce increased passenger volumes on hub-to-hub flight segments.”<sup>176</sup> The airlines must fly frequently between these U.S. and European hubs in order to cover their high fixed costs.<sup>177</sup> Thus, the more passengers they transport across the Atlantic, the greater the cost economies. Remember, airline carriers sell a highly perishable good; once an airplane takes off, the empty seats are completely worthless. However, deregulation has produced the odd paradox of overcapacity in the airline industry.<sup>178</sup> Airlines must fly transatlantic hub-to-hub routes often to cover high fixed costs (fuel, labor, planes, etc.), but each new flight increases the supply of seats across the Atlantic, which in turn lowers fares and decreases revenue.<sup>179</sup>

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172. DOJ Comments, *supra* note 92, at 13 n.36.

173. McQuaid, *supra* note 115, at 682.

174. See Reitzes & Moss, *supra* note 10, at 295–96.

175. *Id.* at 298.

176. *Id.*

177. Warden, *supra* note 11, at 234.

178. *Id.*

179. *Id.*

Enter the airline alliance hub-to-hub model of international aviation.

The airlines had to come up with a way to control the overcapacity paradox and self-regulate the transatlantic market.<sup>180</sup> What actually happened was closer to the airlines carving out markets for themselves.<sup>181</sup> Before the DOT grants antitrust immunity, an international airline alliance is an essentially cooperative venture in which airlines from different countries can coordinate a passenger's itinerary through connecting hubs.<sup>182</sup> In other words, they operate in much the same way that large domestic carriers operate in the United States.<sup>183</sup>

For example, there is no major domestic carrier that operates a direct route from Houston, TX to Roanoke, VA, as such would not be profitable. Rather, a passenger traveling this route will likely have to fly first to another major hub, such as Atlanta, GA and catch a connecting flight on to Roanoke. While there are probably multiple carriers that service the Houston-Atlanta route, there is likely only one that services the Atlanta-Roanoke route, which is a significantly smaller market. As more than one airline likely flies into Roanoke through other hubs, the passenger would have a choice of airlines to choose from in Houston in order to reach his final destination. The benefit of the hub-and-spoke model is that the passenger may instead choose another airline whose route is Houston-Charlotte-Roanoke or Houston-Newark-Roanoke.<sup>184</sup>

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180. *See id.*

181. *See id.* at 238.

182. *See id.* at 237.

183. *See id.* at 235–38 (discussing U.S. domestic carrier operation).

184. This is an example of the hub-and-spoke model: spoke-to-hub-to-spoke. Houston-Atlanta-Roanoke service is offered by Delta through its Atlanta hub. *See* Flight Service from Houston, TX to Roanoke, VA, DELTA AIRLINES, <http://www.delta.com> (follow “Book a Flight” hyperlink; then search Houston, TX for “From” and search Roanoke VA, for “To;” then select a date and follow “Find Flights” hyperlink). *See also* *Route Maps*, DELTA AIRLINES, [http://delta.innosked.com/\(S\(knw1gr55w0uhtyjatbhhsd55\)\)/Default.aspx](http://delta.innosked.com/(S(knw1gr55w0uhtyjatbhhsd55))/Default.aspx) (last visited Feb. 26, 2011) [hereinafter *Delta Route Map*] (showing Delta Airlines’ hub cities). Houston-Charlotte-Roanoke service is offered by U.S. Airways through its Charlotte hub. *See* Flight Service from Houston, TX to Roanoke, VA, U.S. AIRWAYS,

However, if the passenger's final destination were Atlanta, this would create a hub-to-hub itinerary.<sup>185</sup> Obviously, as two of the largest cities in the United States, there is a dense amount of both commercial and leisure traffic, especially around the holidays.<sup>186</sup> This is beneficial to the consumer because there are likely multiple airlines that service the Houston-Atlanta route. In antitrust analysis this is known as horizontal competition.<sup>187</sup> Because airlines in the United States, servicing domestic routes, are subject to antitrust laws, they may not share information with their alliance partners.<sup>188</sup> In other words, every airline is a competitor against every other airline and the market determines fares and capacity.<sup>189</sup>

The major concern of antitrust immunity is the elimination of this horizontal competition in the nonstop, transatlantic hub-to-hub market (e.g., Houston-Paris), where the highest density of passengers is located.<sup>190</sup> Once an alliance, or transatlantic joint venture, has been granted immunity and achieved metal neutrality,<sup>191</sup> the alliance partners have absolutely no incentive to compete with each other between their two international

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<http://www2.usairways.com/Default.aspx> (follow "Book Travel" hyperlink; then search Houston, TX for "From" and search Roanoke VA, for "To," then select "Depart" and "Return" dates and follow "Search Flights" hyperlink). And Houston-Newark-Roanoke service is operated by Continental, as both Houston and Newark are Continental hubs. See *Route Maps, CONTINENTAL AIRLINES*, [http://www.continental.com/CMS/ContinentalDocuments/pdfs/route-maps/co-us\\_201012.pdf](http://www.continental.com/CMS/ContinentalDocuments/pdfs/route-maps/co-us_201012.pdf) [hereinafter *Continental Route Map*] (showing Continental hub cities and their connections with other cities).

185. Houston is Continental's hub and Atlanta is Delta's. See *Delta Route Map*, *supra* note 184; *Continental Route Map*, *supra* note 184.

186. The Atlanta metropolitan area is the ninth most populous region in the country, and Houston is the sixth most populous region in the country. U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: LARGE METROPOLITAN STATISTICAL AREAS: POPULATION (2011), *available at* <http://www.census.gov/compendia/statab/2011/tables/11s0020.pdf>.

187. Reitzes & Moss, *supra* note 10, at 306.

188. See Dan Reed, *American Airlines Expands European Alliance*, USA TODAY, Oct. 6, 2010, *available at* [http://www.usatoday.com/money/industries/travel/2010-10-06-american-airlines-iberia-british-airways-trans-atlantic-alliance\\_N.htm](http://www.usatoday.com/money/industries/travel/2010-10-06-american-airlines-iberia-british-airways-trans-atlantic-alliance_N.htm).

189. See *id.*

190. See Reitzes & Moss, *supra* note 10, at 306.

191. See *supra* notes 62–66 and accompanying text (discussing metal neutrality and airline alliances).

gateways.<sup>192</sup> Thus, if Euro-Air's hub is Paris and Ameri-Air's hub is Houston, neither has incentive to compete on flights between the two hubs, because they overlap.<sup>193</sup> The DOJ has cautioned that "barriers to entry such as airport slots could magnify such effects."<sup>194</sup> Perhaps this analysis alone would not be enough to undermine the U.S.-E.U. Open Skies Agreement and principles of liberalization, which allow airlines to fly freely from one city to another. However, the practice of predatory pricing at these international gateway hubs effectively wards off serious competitors in the nonstop hub-to-hub market.<sup>195</sup>

#### *F. Predatory Pricing*

Predatory pricing in the airline industry is not a new concept.<sup>196</sup> Essentially, the theory is that an airline carrier will protect its home turf, or hub, against new or potential entrants by pricing below its cost or increasing capacity to flood the market and reduce fares.<sup>197</sup> Either way, the goal is to deter entry of new competitors in particular markets (routes) by pricing so low that the new entrant has no option but to exit the market.<sup>198</sup>

A prime example of airline predatory pricing is found in the People Express/Northwest Airlines case before the Civil Aeronautics Board.<sup>199</sup> In that dispute, Northwest was accused of

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192. See *supra* notes 62–63 and accompanying text. This is due to metal neutrality and the revenue sharing agreements between the carriers. See *supra* notes 62–63 and accompanying text.

193. See *supra* Part III.A.

194. Reitzes & Moss, *supra* note 10, at 307.

195. Ruwantissa Abeyratne, *US/EU Open Skies Agreement—Some Issues*, 72 J. AIR L. & COM. 21, 33 (2007).

196. See Roger W. Fones, Chief, Transp., Energy & Agric. Antitrust Div., Dep't of Justice, Remarks before the American Bar Association Forum on Air & Space Law: Predation in the Airline Industry 5–12 (June 12, 1997), available at <http://www.justice.gov/atr/public/speeches/1188.pdf>.

197. *Id.* at 2–3.

198. *Id.* at 3–4.

199. See JAMES LARDNER & ROBERT KUTTNER, FLYING BLIND: AIRLINE DEREGULATION RECONSIDERED 6 (2009), available at <http://www.enotrans.com/vertical/Sites/%7B894F22DF-1788-4CA0-A19C-02688F64CCBE%7D/uploads/%7B73633E65-FFAE-4F40-A81C-E2830507930B%7D.PDF>.

predatory pricing in the nonstop service market from Minneapolis/St. Paul to New York in 1985.<sup>200</sup> Before People Express started servicing this route, Northwest's regular fare was \$263 roundtrip.<sup>201</sup> After People Express started to service the route, Northwest slashed fares to \$99 during peak hours and \$79 during off-peak hours.<sup>202</sup> Even though these fares matched those of People Express, Northwest's status as a "legacy carrier" meant that it was known for more reliable service and had greater brand recognition than People Express, a relatively unproven low cost carrier.<sup>203</sup> Faced with a competitor offering lower prices, more capacity, and greater brand loyalty, People Express had no choice but to exit the Minneapolis/St. Paul-New York market after only six weeks of operation.<sup>204</sup>

Standard U.S. antitrust policy does not make such "predatory pricing" unlawful under the Sherman Act, unless there exists a dangerous probability of recoupment of the predator's losses following the competitor's exit.<sup>205</sup> If the predator cannot recoup his losses plus some additional profit after his competitor exits the market, the predation is not unlawful.<sup>206</sup> In other words, if the alleged predator prices below cost, and does not recover the losses from consumers in the future, then "consumer welfare is enhanced."<sup>207</sup>

The principle that predatory pricing is not unlawful unless recoupment can be proven is a product of the Chicago school of thought on economics.<sup>208</sup> The theory is that predatory pricing is

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200. See James L. Robenalt, Note, *Predatory Pricing in the Low Fare Airline Market: Targeted, Discriminatory, and Achieved with Impunity*, 68 OHIO ST. L.J. 641, 660–61 (2007).

201. LARDNER & KUTTNER, *supra* note 199, at 6.

202. Russell A. Klingaman, *Predatory Pricing And Other Exclusionary Conduct in the Airline Industry: Is Antitrust Law the Solution?*, 4 DEPAUL BUS. L.J. 281, 303 (1992).

203. LARDNER & KUTTNER, *supra* note 199, at 9–10 (discussing the differences between legacy carriers and low cost airlines).

204. *Id.* at 6.

205. See *Brooke Group, Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224–25 (1993).

206. Abeyratne, *supra* note 195, at 37.

207. *Id.* (citation omitted).

208. Jonathan B. Baker, *Predatory Pricing After Brooke Group: An Economic Perspective*, 62 ANTITRUST L.J. 585, 586–89 (1994).

never a rational strategy for a profit maximizing enterprise to engage in, because recoupment is unlikely.<sup>209</sup> However, following the Supreme Court's decision in *Brooke Group*, the post-Chicago school of economics presented some scenarios in which recoupment were not only possible through predatory pricing, but also probable.<sup>210</sup> One such theory advanced by this group of economists is "recoupment by reputation."<sup>211</sup>

The classic example presented under this theory is a case in which American Airlines protected its Dallas-Fort Worth hub from entry by a low cost carrier (LCC) trying to establish its own hub there.<sup>212</sup> In other words, the LCC was trying to "force" its way into the DFW hub by offering almost identical service as American but at lower prices. The possibility of a competitor LCC establishing a hub at the same location as American's triggered a predatory response; American matched the LCC's fares and dumped capacity—using larger planes more frequently—on contested routes.<sup>213</sup> Once American successfully fended off the LCC through predatory pricing, it earned a reputation in the industry as willing to crush the competition, in the event any other airlines tried to enter the DFW market in the future.<sup>214</sup> In effect, American engaged in predatory pricing, via its reputation, against potential competitors without having to reduce its fares.<sup>215</sup> Thus, American "recouped its losses" without actually losing anything.<sup>216</sup> American defended its hub against competition and discouraged new airlines from challenging it in the future.

Now apply these principles on a global scale to the international airline alliances and their dominated hubs. It is likely that the three major alliances dominate their respective

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209. *Id.*; *United States v. AMR Corp.*, 335 F.3d 1109, 1114 (10th Cir. 2003).

210. *Baker*, *supra* note 208, at 589–90.

211. *Id.* at 590.

212. *AMR Corp.*, 335 F.3d at 1111–12.

213. *Id.* at 1112–13.

214. *Id.* at 1114. This theory assumes that American Airlines priced below the monopoly price before the LCC entry, but would be able to charge a true monopoly price once it gained a reputation as a predator. *See id.*

215. *See id.*

216. *See id.*

hubs located in the United States and European Union. For example, return to the hypothetical involving Euro-Air and Ameri-Air.<sup>217</sup> Assume that the two airlines are part of the same alliance and also have a transatlantic joint venture with antitrust immunity granted by the DOT and the European Commission. Further assume that there are only two other competing immunized alliances with their respective hubs in different cities. A passenger traveling from Houston to Paris, wishing to fly nonstop, will likely only have one option: a plane that is part of the Ameri-Air/Euro-Air alliance. Since the two airlines have a revenue sharing agreement in place, it does not matter to them which airline actually services the flight, as they collect the same amount of revenue either way. Further, the alliance will try to protect its hubs by any means necessary, including predatory pricing and capacity flooding. However, since the alliance has obtained antitrust immunity, the member airlines are free from prosecution by the DOJ for such practices.

Thus, the hub-and-spoke model of airline alliance transatlantic aviation, coupled with antitrust immunity and predatory pricing tactics to protect key continental hubs, seriously undermines the effectiveness of the U.S.-E.U. Open Skies Agreement. While the Agreement is meant to liberalize the transatlantic market and increase the possibility of competition,<sup>218</sup> the whole point is moot if the alliances are granted immunity from the antitrust laws. In other words, if airline alliances can only fly to their respective alliance hubs, either in the United States or in the European Union, due to predatory pricing or the reputation of predatory pricing, do they really have the choice to fly from “any point in the U.S. to any point in the E.U. and vice versa”?<sup>219</sup> Probably not. It is more likely that a system will develop where consumers have the option to fly nonstop to only six different cities back and forth

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217. See *supra* Part III.E.

218. U.S.-E.U. Open Skies, *supra* note 3, at pml.

219. U.S.-E.U. Open Skies Agreement: With a Focus on the U.S. Department of Transportation’s Notice of Proposed Rulemaking (NPRM) Regarding Actual Control of U.S. Air Carriers: Hearing Before the Subcomm. on Aviation of the H. Comm. on Transp. and Infrastructure, 109th Cong. 12 (2006) (statement of Rep. Boswell, Member, H. Comm. on Transp. and Infrastructure).

across the Atlantic; three cities in the European Union and three cities in the United States, all dominated by immunized alliances. Liberally granting antitrust immunity to alliances does not promote international aviation competition;<sup>220</sup> it destroys it.

### *G. Collusion*

Another fear to consider in granting antitrust immunity is the possibility of collusion amongst competitors.<sup>221</sup> This fear is particularly strong when “two or more U.S. carriers become members of the same immunized alliance.”<sup>222</sup> Thus, these anticompetitive effects are especially troublesome regarding the Star Alliance, now that it has three U.S. carrier members: Continental, United, and U.S. Airways.<sup>223</sup> While the DOT conferred antitrust immunity on the alliance, the immunity only extends to international route cooperation, and the fear that there may be some “anticompetitive spillovers into domestic markets” is very real.<sup>224</sup> As stated previously, airlines that have a joint venture agreement and receive antitrust immunity can share extremely sensitive information relating to pricing policies, capacities, traffic flow, and scheduling.<sup>225</sup> While this allows a greater level of integration and cooperation for the U.S. carriers on international ventures, it also makes monitoring the joint ventures between the U.S. carriers a nightmare for the DOT and the DOJ.<sup>226</sup>

However, collusion worries do not end on the domestic front. With the advent of alliances, and with more and more airlines joining them, it appears that the transatlantic market is shrinking to only three competitors—the three alliances.<sup>227</sup> The

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220. U.S.-E.U. Open Skies, *supra* note 3, at pmb1.

221. See Reitzes & Moss, *supra* note 10, at 308.

222. *Id.*

223. See A++ Final Order, *supra* note 85, at 1; STAR ALLIANCE, *supra* note 51.

224. Reitzes & Moss, *supra* note 10, at 308; A++ Final Order, *supra* note 85, at 28–29.

225. See *supra* Part III.A–B.

226. Reitzes & Moss, *supra* note 10, at 308.

227. 155 Cong. Rec. E190 (daily ed. Feb. 3, 2009) (statement of Rep. James L. Oberstar).

risk of collusion and price-fixing is greatly enhanced in concentrated markets where there are only two or three firms.<sup>228</sup> Since the transatlantic market is shaping into a three-firm market, the possibility of cooperation between the three alliances to set a “universal” transatlantic fare is of great concern.<sup>229</sup>

#### IV. RECOMMENDATIONS

##### A. *H.R. 831: Rep. Oberstar’s Bill*

The frequency with which the DOT has granted requests for antitrust immunity has drawn the attention of some in Washington, D.C.<sup>230</sup> House Resolution 831, introduced by former Representative Oberstar, contains some insightful proposed solutions to the diminished competition among transatlantic aviation.<sup>231</sup>

First, the bill directs the U.S. Government Accountability Office (GAO) to conduct studies on the procedures used by the DOT in granting antitrust immunity to airline alliances, and to determine whether such procedures conform to U.S. law under sections 4138 and 4139 of the Transportation Code.<sup>232</sup> Under those statutes, the DOT is permitted to grant antitrust immunity only when it is “required by the public interest” and when the predicted public benefits “cannot be achieved by other means.”<sup>233</sup>

Second, the bill directs the GAO to determine whether, and to what extent, immunized alliances have actually produced public benefits and whether these benefits could be produced

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228. Eralp Bektas, *Test of Market Structure and Profitability in Liberalizing the Deposit Market: The Case of North Cyprus*, 4 PROBS. & PERSP. IN MGMT. 62, 62–63 (2006), available at [http://www.businessperspectives.org/journals\\_free/ppm/2006/PPM\\_EN\\_2006\\_02\\_Bektas.pdf](http://www.businessperspectives.org/journals_free/ppm/2006/PPM_EN_2006_02_Bektas.pdf).

229. See 155 Cong. Rec. E190–91.

230. See *id.*

231. *Id.* at E191.

232. H.R. 831, 111th Cong. § 1(a) (2009).

233. 49 USC §§ 41309, 41308 (2006).

without the grant of antitrust immunity.<sup>234</sup> This Comment has suggested that many benefits of international airline alliances, such as frequent flyer reciprocity, checked through ticketing and baggage transfer, lounge sharing and many others, can be achieved without the grant of antitrust immunity.<sup>235</sup>

Mr. Oberstar's bill also directs the GAO to determine which agency—the DOT or the DOJ—is more qualified to grant antitrust immunity to airlines.<sup>236</sup> As a practical matter, it seems that either the DOJ's Antitrust Division or the Federal Trade Commission is more knowledgeable than the DOT in the area of antitrust policy and enforcement. Notably, since 2003, the DOT and DOJ have differed considerably in their opinions on whether and to what extent immunity should be granted.<sup>237</sup>

The bill also suggests that granting immunity to an alliance should be treated comparably to a merger and thus should be subject to the scrutiny of the DOJ.<sup>238</sup> This solution makes a great deal of sense, because international airline alliances are, realistically, an international merger of airlines.<sup>239</sup> Were it not for the U.S. foreign ownership restrictions, it is unclear whether alliances would even exist today, as airlines would likely just merge or create non-immunized reciprocity agreements.<sup>240</sup>

Most importantly, the Oberstar bill contains a mandatory sunset provision.<sup>241</sup> The bill requires that any immunity from the antitrust laws granted by the DOT is to automatically expire three years after the initial grant or subsequent renewal.<sup>242</sup> Only after a reapplication and reevaluation of the alliance's competitive situation would the DOT be allowed to renew

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234. H.R. 831 § 1(b)(1).

235. *Supra* Part III.A; DOJ Comments, *supra* note 92, at 4.

236. H.R. 831 § 1(b)(7).

237. *See generally* DOJ Comments, *supra* note 92, at 13–15 (strongly disagreeing with the DOT that a grant of immunity in the Star ATI case would result in public benefit).

238. H.R. 831 § 1(b)(8).

239. Show Cause Order, *supra* note 85, at 6.

240. *See id.*

241. H.R. 831 § 1(e).

242. *Id.*

antitrust immunity.<sup>243</sup> This method is much more preferable to the current practice of granting perpetual immunity until retraction by the DOT.<sup>244</sup>

This bill should be passed by Congress to alleviate many of the concerns with antitrust immunity addressed in this paper. At the minimum, the GAO study advocated in the bill will better inform Congress and the American public of exactly what benefits they are receiving by exempting these alliances from U.S. antitrust laws.

### *B. Phase II of the U.S.-E.U. Open Skies Agreement*

One major justification to the formation and immunization of airline alliances is the foreign ownership restriction placed on U.S. airlines by Congress.<sup>245</sup> While the European Union does have some restrictions, it is likely that they are a response to those found in the United States.<sup>246</sup> In fact, Article 21 of the Open Skies Agreement explicitly calls for negotiations of “additional foreign investment opportunities.”<sup>247</sup> A major crutch used by U.S. airlines in their applications for immunity are the harsh economic conditions facing the airline industry, as well as rising fuel costs.<sup>248</sup> The European Union needs to demand allowances from the United States on foreign ownership, so that citizens and corporations of other countries can pump much needed capital into the distressed U.S. airline industry.

The United States controls a dominant position in the international airline industry, thanks to its protectionist policies and its persuasion of European countries to agree to Open Skies agreements.<sup>249</sup> However, U.S. airlines have recently been plagued by record losses in both the international and domestic markets, which have triggered bankruptcy filings by even legacy

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243. *Id.*

244. See 155 Cong. Rec. E190 (daily ed. Feb. 3, 2009) (statement of Rep. James L. Oberstar).

245. Reitzes & Moss, *supra* note 10, at 304.

246. Benoit M. J. Swinnen, *An Opportunity for Trans-Atlantic Civil Aviation: From Open Skies to Open Markets?*, 63 J. AIR L. & COM. 249, 274 (1997).

247. U.S.-E.U. Open Skies, *supra* note 3, at art. 21(2)(b).

248. See Joint Application, *supra* note 111, at 3.

249. Warden, *supra* note 11, at 227, 238–39.

carriers.<sup>250</sup> These bankruptcies, coupled with skyrocketing fuel prices, closely followed government bailouts of several U.S. legacy carriers.<sup>251</sup> The solution is not more regulation. Rather, the European Union needs to pressure the United States to open its airlines to foreign capital, both to keep U.S. carriers afloat and to move towards a market-based global aviation scheme—a world where competition flourishes because consumers are protected by their antitrust laws, not where competitors flourish because antitrust immunity laws protect them.

## V. CONCLUSION

In conclusion, the recent formation and consolidation of international airline alliances may have negative impacts on transatlantic competition. Particularly with the addition of Continental Airlines to the STAR ATI alliance, creating one alliance composed of three major U.S. airlines, the door to anticompetitive conduct, such as collusion and predatory pricing, may now be open. The DOT's generous grants of antitrust immunity to these alliances have effectively concentrated the transatlantic market down to three firms—the major airline alliances.

This form of systems competition, the hub-and-spoke model, creates serious anticompetitive concerns as alliances protect their respective hubs through predatory pricing or the threat of pricing below cost. Such a system does not allow for a deregulated transatlantic market, as envisioned by the U.S.-E.U. Open Skies Agreement. Taken together, these conditions seriously undermine the purpose and effect of the U.S.-E.U. Open Skies Treaty.

In order to combat these anticompetitive effects, the United States must pass HR Bill 831, including a sunset provision on all grants of antitrust immunity. Further, the United States and the European Union need to continue with Phase II of their Open Skies negotiations and allow for more opportunities for foreign investment in the U.S. airline industry.

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250. See McQuaid, *supra* note 115, at 670.

251. Dan Reed, *High-Priced Fuel Scars Airlines*, ABC NEWS, Mar. 24, 2008, <http://abcnews.go.com/Business/story?id=4517584&page=1>.