S. HRG. 107–1094

EFFECTS OF THE AMERICAN AIRLINES/TWA TRANSACTION AND OTHER AIRLINE INDUSTRY CONSOLIDATION ON COMPETITION AND THE CONSUMER

HEARING

BEFORE THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

FIRST SESSION

FEBRUARY 1, 2001

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SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

ONE HUNDRED SEVENTH CONGRESS

FIRST SESSION

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EFFECTS OF THE AMERICAN AIRLINES/TWA TRANSACTION AND OTHER AIRLINE INDUSTRY CONSOLIDATION ON COMPETITION AND THE CONSUMER

THURSDAY, FEBRUARY 1, 2001

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Committee met, pursuant to notice, at 9:32 a.m. in room SR–253, Russell Senate Office Building, Hon. John McCain, Chairman of the Committee, presiding.

OPENING STATEMENT OF HON. JOHN McCAIN, U.S. SENATOR FROM ARIZONA

The CHAIRMAN. Good morning.

Eight months ago, United Airlines announced its intention to merge with US Airways, potentially creating the largest airline in the world. At that time I expressed my strong reservations about the proposal. I was concerned that the proposed transaction would lead to further industry consolidation, which would have a detrimental effect on competition and in turn the consumer. As a result, this Committee passed a resolution disapproving the United-US Airways merger.

Four months ago, the chairmen of the second and third largest airlines in the U.S., American and Delta Airlines respectively, sat in front of this Committee and warned that they would be forced to react to the proposed United-US Airways mergers, if approved, to remain competitive. Today, one of them, American, is here to discuss its proposed actions that would make American comparable in size to United if the currently proposed transactions are approved. This would result in two airlines controlling approximately 50 percent of the U.S. market.

It comes as no surprise that current news reports indicate that Delta is involved in negotiations with both Northwest and Continental in order to remain competitive in light of these proposals. The move by Delta could result in three major airlines controlling an estimated 75 percent to 85 percent of the U.S. airline market, the very situation that I and others predicted 8 months ago.

I do not know of any one other than the airlines who thinks that a “big three” industry is good for the consumer. The airlines tout network benefits and seamless travel as a benefit to the consumer. Maybe I am mistaken, but I thought it was competition that was good for the consumer. That is something that there would be little of if these transactions all come to fruition.

These big three will control markets, gates, and access to facilities. They will have the pricing power to slowly force out or severely constrict the growth of new entrants. The consumer is the one who will pay the price.

A "big three" industry also gives labor increased leverage to disrupt service. We need only to look at United's problems last summer and Delta's and Northwest's current problems. If labor disruptions occur at a consolidated United or American, the rest of the system will not be able to absorb the displaced passengers and the system will grind to a halt.

I believe that the issue before us this morning, before the Committee, is an important one. I believe that if we continue these mergers and consolidations that the consumer will suffer. I do not fault CEO's of the airlines for seeking these mergers and consolidations. That is their business. But it is the business of the Congress to see that the consumer is not left out and that the consumer is able to enjoy the benefits of the promise of airline deregulation, which was less regulation, more entrants into the markets, and consequently lower prices to the consumer.

[The prepared statement of Senator McCain follows:]

PREPARED STATEMENT OF HON. JOHN MCCAIN, U.S. SENATOR FROM ARIZONA

Eight months ago, United Airlines announced its intention to merge with US Airways, potentially creating the largest airline in the world. At that time, I expressed my strong reservations about the proposal. I was concerned that the proposed transaction would lead to further industry consolidation which would have a detrimental effect on competition and, in turn, the consumer. As a result, this Committee passed a resolution disapproving the United/US Airways merger.

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It comes as no surprise that current news reports indicate that Delta is involved in negotiations with both Northwest and Continental in order to remain competitive in light of these proposals. A move by Delta would result in three major airlines controlling an estimated 75 to 85 percent of the U.S. airline market, the very situation that I and others predicted eight months ago. I don't know of anyone, other than the airlines, who thinks that a "big 3" industry is good for the consumer.

The airlines tout network benefits and "seamless travel" as a benefit to the consumer. Maybe I am mistaken, but I thought it was competition that was good for the consumer. And that is something that there will be little of if these transactions all come to fruition. These "big 3" will control markets, gates and access to facilities. They will have the pricing power to slowly force out or severely constrict the growth of new entrants. The consumer is the one who will pay the price.

A "big 3" industry also gives labor increased leverage to disrupt service. We need only to look at United's problems last summer and Delta's and Northwest's current problems. If labor disruptions occur at a consolidated United or American, the rest of the system will not be able to absorb the displaced passengers and the system will grind to a halt.

Mr. Compton, I recognize the benefit of this acquisition to your company and employees. Senator Carnahan, I also recognize the benefit to your state and the city of St. Louis. However, the airline industry is facing a crisis right now. The report authored by our current Secretary of Transportation, Secretary Mineta, sets out some good ideas to fix the system. I personally believe the answer is to pour more concrete, increase competition and fix the air traffic control problem. We are at a crossroads and have a tremendous opportunity to take steps to address these issues.

I cannot help but believe that a "big 2" or "big 3" consolidated airline industry will limit this opportunity and make the current situation even worse.

I thank the witnesses for their time and look forward to their testimony.

The CHAIRMAN. Senator Hollings.

STATEMENT OF HON. ERNEST F. HOLLINGS, U.S. SENATOR FROM SOUTH CAROLINA

Senator HOLLINGS. Thank you, Mr. Chairman. I will just ask that my statement be filed.

[The prepared statement of Senator Hollings follows:]

PREPARED STATEMENT OF HON. ERNEST F. HOLLINGS, U.S. SENATOR FROM SOUTH CAROLINA

Good morning. Last year, we held two days of hearings alone on the proposed United-US Airways merger to examine its market implications. Testimony was received from industry and government officials as well as industry experts. The main concern was that the acquisition would open the floodgates, and set off a host of other massive mergers. Well that concern has become a reality. We all knew that the United-US Airways-DC-Air transaction would lead to other deals. We have them today. Just yesterday the Wall Street Journal noted the current negotiations involving Northwest, Continental and Delta. No doubt we're going to end up with three carriers controlling fortress hubs across the country.

What we do not have is anyone looking out for the public interest. The Department of Justice will review these deals market by market, inch by inch. Without any notion of the big picture. The fact is that we need competition at each of the fortress hubs. Why should we continue to allow a carrier with 60, or 70 percent of the traffic at a major city to stifle entry, control gates and other assets needed to provide meaningful competition. In other critical sectors of our economy, telecommunications, for example, we have limits on media ownership enabling others to provide information and services. I want the Department of Transportation to have that ability—to be able to say "we need more service, more competition in specific markets, less hub domination, less slot domination". It simply is time that the traveling public got its say.

We also have had study after study telling us that there are real, and serious, competitive problems within the air transportation system. Fortress hubs, market domination, predatory pricing—these are the terms we see and read about in the studies. I know there are benefits to the hub system as some communities, particularly the smaller ones, get more service than they otherwise would, but it comes at a price—a very high price. I have said that I do not like deregulation, and that the regulated are taking over the regulated, as the European carriers attempted to buy into the U.S. market, but that has slowed down in recent years. Northwest has its arrangement with KLM, for example. What we see today is the deregulated taking over the deregulated, and the top 3 looking to get even bigger.

Today, though, we will focus on the deregulated merging and consolidating. Network efficiencies, we are told will provide us bigger and better service. The GAO and Mr. Levine, supported by Department of Transportation's studies, can tell us that bigger is not better. DOT in fact has found that fares are 41 percent higher in markets without competition, and even higher for smaller, shorter haul markets (54 percent).

I should note that American has come to TWA's rescue, which I support. It will save jobs, and protect consumers who would have lost service. I have heard from pilots at TWA that they support American's bid.

The rest of the proposed mergers, however, fall or succeed together. United's deal with US Airways clearly ran into DOJ concerns,—regarding United's relationship with DC Air, in addition to its, hub to hub routes, and the shuttle operations. American has now been invited to come along and correct these problems. But should it be American, and not a low cost carrier? Unfortunately, DOJ is likely to decide that hub to hub competition is great and possibly clear these transactions. The key, but unanswered question, however, is what happens to consumers. American and DC Air, with their marketing arrangement, jointly will control 51 percent of the slots at Washington National Airport. United will operate and dominate hubs at Dulles, Pittsburgh, Philadelphia, Charlotte, Denver, and San Francisco. United today derives a large percentage of its revenues from the East Coast, almost 35 percent of its total revenues. Thus, while they assert that they need to purchase US Airways to gain a foothold, they downplay that they already have an enormous presence in the East.

What they get out of the arrangement is control, not an increase in hub domination, but control of more hubs. Ultimately, the more hubs you control, the more you can control the number of seats in the markets and the prices. Is this what deregulation was suppose to give us? I hope not. It is clear that the word "competition" is lacking. Look at the Wall Street analyst reports. One report noted in discussing the United-American-US Airways merger that "This reminds us of a funny story about how fewer, but bigger national airline networks will compete even more vigorously with each other than they do today." Is this the type of market we want for the American people?

Regarding TWA. It clearly was a pretty good airline. It leased new planes, had a good on-time performance rating and provided good service. Without American's efforts, TWA would have been forced to close its doors, leaving thousands of employees out of work, and more important, thousands of travelers without service. The point is that we are not losing a competitor that would not have been lost anyway.

What we need to ensure is that other carriers have the ability to get into the fortress hubs. Barriers to entry must be torn down, with limits on a carrier's ability to own or control assets at our major hubs. We should no longer permit airline contracts that inhibit entry at airports. We also ensure that no more airport grant monies or passenger facility charges be allowed unless the fortress hubs agree to expand to accommodate competition. All of these elements should be part of the public interest. It is our job, and we will make it the job of DOT, to protect the travelers.

Alfred Kahn testified in 1998 before this Committee that "Deregulation makes sense and can only continue in the presence of effective competition as the protector of consumers". We need that competition now more than ever. I will listen carefully to the witnesses attempts to explain how less equals more.

The CHAIRMAN. Thank you.

We welcome our colleagues this morning. Can we begin with Congresswoman Slaughter if that is agreeable, since she came all the way across the Capitol to be with us this morning. Thank you.

STATEMENT OF HON. LOUISE MCINTOSH SLAUGHTER, U.S. REPRESENTATIVE FROM NEW YORK

Ms. SLAUGHTER. Thank you. Thank you, Mr. Chairman. I was delighted to do it, and I want to thank you again for your hospitality. This is the second time I have appeared before your Committee on this same issue.

These hearings particularly come at a critical time, and I do praise your leadership on this issue. I want to say good morning to the other Members of your Committee.

Mr. Chairman, today we are seeing the end game, I think, to an experiment that began 20 years ago when Congress voted to deregulate the airline industry. These mergers are the final act and, should they go forward, it will mean the death knell for an ambitious plan that failed to deliver the promised benefits of more airlines, better service, and cheaper prices that Congress promised to all the American people, not just those living in the popular destinations.

The GAO report that I, along with my colleague James Oberstar of Minnesota, requested made clear in December that the proposed US Airways-United merger would trigger further consolidation of the industry, thereby reducing the industry to as few as three major carriers. That prediction has come true faster than any of us had imagined.

It appears that the mere possibility of a United-US Airways merger has prompted American airlines to buy Trans World Airlines, and now press reports indicate that Delta, Continental, and Northwest are also exploring a strategic alliance.

Mr. Chairman, I am here to urge you to send a clear signal to the Administration that Congress does not want these mergers to go forward. We all sympathize with TWA's workers and we understand their fear of job loss, and we should work together to mitigate any labor disruption. But my district of Rochester, New York, has already seen thousands of jobs lost because businesses move out when they cannot afford our high air fares. We have the fourth highest fares in the United States even though we have many Fortune 500 companies and export more from our region than all but nine of the United States.

Our source of price competition has been jetBlue Airways, a low fare airline which we managed to attract to Rochester last year. But the low-cost carriers like jetBlue, Southwest, or AirTran will find themselves at the mercy of these megacarriers should they take over the domestic aviation market.

Every independent analysis has concluded that these mergers will erode what little competition remains in the aviation industry. With fewer airlines competing against each other, passengers can expect higher prices, fewer flights, and even worse service than they endured over the recent holiday season.

Generations of American taxpayers have poured their hard-earned tax dollars into building our nation's aviation infrastructure and they deserve better. These same taxpayers now find themselves at the mercy of the marketing department of megacarriers who can decide with impunity which regions of the country will live or die based on their access to air service.

I have testified before your Committee in recent years and spoken to you individually about problems facing the flying public. But the public is fed up. They are fed up with both the airlines and Congress' willingness to play the role of handmaiden to major carriers. Let us be frank. The industry gave $6.5 million to members during this election cycle. A pattern has now developed that does not reflect well on Congress. Legislation is proposed, hearings are held, dueling press conferences emerge, and at the end of the day the leadership backs away from any real action, promising further study and delivering hollow promises.

Mr. Chairman, we have studied this issue to death. The time we have wasted has brought us to a point where three carriers are poised to dominate the entire domestic aviation market. If we do not act, the public will rightly view this institution as part of the problem, rather than the solution.

I thank the Committee for their time and attention, and I appreciate your great concern, Mr. Chairman, on this issue.

The CHAIRMAN. Thank you very much, Congresswoman Slaughter. You are always welcome here and we appreciate all of your efforts.

Senator Bond, welcome.

STATEMENT OF HON. CHRISTOPHER S. BOND, U.S. SENATOR FROM MISSOURI

Senator BOND. Thank you very much, Mr. Chairman, Senator Hollings, Members of the Committee.

I ask unanimous consent that the full statement be included in the record.

The CHAIRMAN. Without objection.

Senator BOND. I just want to tell you a couple things. I want to tell you a little story about my friends at TWA. Number 1, I commend you for your efforts to assure competition in airlines. The failure of competition where there has been deregulation has been a problem in many other areas, and I commend you for your efforts.

But let us make one thing clear. This is not about maintaining competition by preventing merger between two viable carriers. This is a matter of life and death for the people that are served by TWA, the communities who are served by TWA, and the people who work for TWA.

TWA has a long and proud tradition. It started off as Western Air in 1925, in 1930 became Transcontinental and they started running a mail route through St. Louis. I have not been flying with them since 1930, but I have been flying with them since about 1950, and they are the essential carrier, the major dominant carrier in St. Louis.

They have been through some tough times. Back in 1985 and 1986 when I was out of office before I came to the Senate, I was approached by employees of TWA who wanted to take over the airline, which was up for sale, and prevent it from being stripped. Well, we fought some good battles. The employees did not get funding at the time, so my law firm did not get paid, but it was a good battle.

It was taken over by a man who sold off routes and put some real financial burdens on it. In 1992 the airline almost did not come out of bankruptcy because the Pension Benefit Guaranty Corporation wanted a huge sum to cover the pension costs. I asked the PBGC members to review the impact of putting out of business at that point a 28,000-person airline. I said: You ought to make that a more reasonable cost. They came up with a reasonable plan.

They got TWA out, but they did not get it out in condition to survive financially. We have watched as the new president, a pilot, Bill Compton, has made this one of the finest, most consumer or flyer-friendly airlines around. J.D. Power said it is a great airline. The problem is they did not have the cash behind it. They have to pay 150 percent of what other airlines pay for leases because their credit was not good. They had an arrangement with a prior owner who could sell discount tickets, so the airline was always full, but they were not always getting the money from it. Then the cost of fuel rose.

Well, we had probably the last hurrah of TWA, when it brought back the world champion St. Louis Rams to the TWA Dome after last year's Superbowl. But then things started going downhill. We're now in a position where TWA either goes into bankruptcy, ends its service, splits up and gets picked off by more vultures what want to pick and choose little pieces of it, or whether we go through with the arrangement proposed by American Airlines that will keep the airline flying and keep the service that is needed for me and the other hundreds of thousands of flyers who use the 1,000 flights a day out of St. Louis.

We need to keep the 9,000 employees of TWA working in St. Louis, the 3500 who work in Kansas City. This is an opportunity for the bankruptcy courts to make good service available and serve consumers. It is not going to have any harm, it is not going to cause any harm to Rochester or Schenectady or any other place. This is an airline that is going to go under and go out of business unless the bankruptcy court can approve the sale.

Right now TWA is a debtor-in-possession and had it not been for the infusion of cash they would have been out of business. The airline industry, the airline consumers, and certainly the State of Missouri do not need to go through another disaster wiping out another airline altogether. We have seen that in Kansas City with Braniff and with Eastern. The results have been disastrous.

We have here today an opportunity for a shining knight on a white steed to come in and keep airline service going that is important not only for the hub, but for the many smaller communities in the Midwest served by TWA. It may not be TWA any longer, but at least the service will be there, the communities will have the economic opportunities of good air service, and the employees will be able to continue to do the excellent job they have done of serving the nation's airline travelers.

I thank the chair.

[The prepared statement of Senator Bond follows:]

PREPARED STATEMENT OF HON. CHRISTOPHER S. BOND, U.S. SENATOR FROM MISSOURI

Good morning, Mr. Chairman, Senator Hollings, and fellow colleagues. I thank the Chairman and the Committee for holding this hearing, and am pleased to appear before you to discuss the potential acquisition of Trans World Airlines by American Airlines, the impact on my home State of Missouri, and issues related to airline competition.

History of TWA

Let me start by providing some brief history of one of the most famous names in aviation and the longest-flying carrier in American commercial aviation, Trans World Airlines or TWA. For years TWA was associated with the big names, big planes, and great service. It is sad to see those days come to an end.

TWA's beginnings go back to 1925 when it was known as Western Air Express. It quickly evolved into Transcontinental Air Transport or the "Lindbergh Line" due to Charles Lindbergh's involvement with the airline. It was Transcontinental, that was headquartered in Kansas City, Missouri, that laid out the first coast to coast air and rail route in 1929.

A year later, in 1930, the federal government decided that airlines could and should carry more people than mail and the transcontinental lines emerged with what would become United, American, TWA, and Eastern. TWA had the central route through St. Louis, Missouri and TWA has had a major airline presence in St. Louis, Missouri ever since.

Another interesting airline fact, and one that I like, is that St. Louis is the birthplace of one of today's leading airlines. It is not TWA, but American Airlines, whose earliest predecessor company—Robertson Aircraft Corporation—launched its first airmail flight from St. Louis to Chicago on April 15, 1926.

TWA Has Been A Survivor

Throughout the history of TWA, the airline has had its major ups and downs. A TWA plane crash in Kirksville, Missouri in 1935 killed U.S. Senator Bronson Cutting of New Mexico which served as the catalyst for the creation of the Civil Aeronautics Board. Howard Hughes was brought in the late thirties to help address the growing financial needs. By 1940, Hughes owned the company which lasted until 1965. Even though Hughes increased the name recognition of TWA, throughout his years of ownership he created a fair amount of difficulties that led to a financial drain on TWA. TWA was able to weather that storm and often led the airline industry in profits in the 1960s.

In the 1970s, along came deregulation and TWA was not prepared. The good 'ole days of TWA disappeared. The constant struggle of survival began.

Mr. Chairman, I have been through the struggles of TWA for many years now. As a Governor, a lawyer, and here in the United States Senate, I have answered TWA's calls for assistance. I was involved during the Icahn era which left TWA gasping for breath. I have been through two previous bankruptcies questioning day to day whether or not TWA would be in the air. We all listened in horror about the TWA Flight 800 crash.

The newspaper headlines over the years give an example of the tense situation TWA was under.

"TWA Unveils Plan to Halve Its Debt"—December, 1994

"TWA Bailout 10 Times Bigger Than Announced"—March, 1995

"For Trans World Airlines, It's Chapter 11 Again"—June, 1995

"Auditors Gloomy on TWA's Prospects"—March, 1997

"TWA Juggles Top Executives After Treading in Read Ink for a 10th Straight Year"—March 1999

Time after time, TWA pulled it through. Time after time, TWA was a survivor. Those days are no longer. Unfortunately, despite the heroic efforts of TWA's employees and current management team, it is now clear that the airline can no longer survive.

TWA's Importance to Missouri

Mr. Chairman, if I could have my way, TWA would continue to be a survivor and once again be on top leading the way for other airlines to follow. Unfortunately, as is the case too often, I am not getting my way. The loss of the TWA name in the airline industry is disappointing, but more specifically, the loss of TWA and its operations to my home state of Missouri, would be huge.

TWA has approximately 20,000 employees today. Approximately 9,000 of those employees live and work in the St. Louis, Missouri metropolitan area making TWA the seventh-largest employer in the St. Louis area. At St. Louis Lambert International Airport, TWA operates almost 1000 flights (departures and arrivals) per day.

In Kansas City, Missouri, TWA offers 10 daily flights to St. Louis. TWA employs 3,500 people in Kansas City, including 2,500 at the Kansas City overhaul base.

TWA's headquarters are in St. Louis, Missouri. TWA's support in the community has been apparent by the financial assistance provided locally. Having TWA's St. Louis hub has proven to be a tremendous economic benefit for the St. Louis metropolitan area and the entire State of Missouri.

American Airlines Acquisition

I am not going to deny it. Almost everyone involved with TWA looks at the acquisition of TWA by American Airlines as the knight in shining armor riding in on his white horse rescuing the damsel in distress. For TWA, for TWA employees, for St. Louis, for Kansas City, for the entire State of Missouri, and for the traveling public—this is the only option for us.

American Airlines is offering TWA, the TWA employees, Missouri, and the traveling public a "global" solution. American Airlines has an acquisition plan that will keep TWA flying in the short-term, protect almost all of the 20,000 jobs, maintains the St. Louis hub, maintains the Kansas City overhaul base, and maintains a competitive airline presence in St. Louis into the future. Obviously, this is good news for us—the State of Missouri simply has too much at stake to lose those economic engines.

American Airlines, in my view, has presented the best possible option. In fact, had American not provided immediate financing to TWA in early January, the carrier would have had to shut down, precipitating an economic crisis in Missouri. Likewise, air service from St. Louis to small and mid-sized cities throughout the Midwest would have been disrupted. Indeed, the loss of the St. Louis hub would in the long run, I believe, do significant harm to the airline industry and the hundreds of thousands of air travelers who depend on St. Louis Lambert as their connecting airport.

American Airlines wants the whole pie, not just a slice. That is imperative for TWA, TWA employees, Missouri, and the traveling public.

The Final Chapter

Let's be honest. There are some other airlines who are not happy with this American acquisition of TWA. Almost all of those airlines have considered at one time or another, the purchase of TWA, including US Airways, Northwest, Continental, and Delta. They all passed the opportunity by. At one time, acquiring TWA would have only been a liability. That is not the case today. Captain Bill Compton and his team, including the 20,000 employees, have led the turnaround of TWA, from an airline that nobody wanted to one that they now want to squabble over.

In the past four years the employees of TWA have built their airline into an industry-leading operator—going from last in on-time performance to first, winning numerous customer service awards. In addition, TWA undertook an ambitious program of fleet renewal leaving behind one of the newest fleet's in the industry.

Unfortunately, despite the sterling success of the operational turnaround, continuing financial problems have overwhelmed TWA. Let me be clear. TWA is not crying wolf! Because of the inability to overcome the financial woes which were further burdened by high fuel costs, TWA would have ceased operations mid-January. This is where the knight on the white horse came in.

Mr. Chairman, I understand and share many of the concerns of my colleagues with regard to increased consolidation in the airline industry. The proposed deals between United, US Airways, American, and DC Air raise significant questions in that regard and should be very carefully scrutinized. However, I urge my colleagues not to mix those larger, more complex deals with the American transaction with TWA. To do so will only cause delay and put thousands of jobs at risk in the State of Missouri.

One final point I should make about the proposed arrangement between American Airlines and TWA is its effect on competition, or more particularly the antitrust laws. I confess to having been an antitrust lawyer in my private life; it was the practice of that law that drove me into politics. I do recall, however, some of the main principles of antitrust law, and I am particularly drawn in this situation to the failing company doctrine. This is not an instance where competition is going to be decreased by the transaction between American Airlines and TWA; it is one which will enable the service provided by TWA to continue. Mr. Chairman, this is a glorified estate sale.

Indeed, the on-going bankruptcy proceeding as well as TWA's relatively small size (only 3.9 percent market share) make the American/TWA transaction fundamentally different from the larger deals. It must be resolved swiftly through the bankruptcy court and cleared by the Justice Department to ensure the continued, long-term employment of the thousands of TWA employees in my State of Missouri and those elsewhere in the country.

I hope and trust that the reviewing authorities will not inhibit this transaction from going forward, and I would strongly urge my colleagues not to take any steps that might interfere with this effort to save the service and the jobs of TWA.

Thank you for the opportunity to be here today. I look forward to working with you on this and many other issues.

The CHAIRMAN. Thank you very much, Senator Bond. Thank you for being here this morning.

Senator DeWine.

STATEMENT OF HON. MIKE DEWINE, U.S. SENATOR FROM OHIO

Senator DEWINE. Mr. Chairman, thank you very much. Let me congratulate and thank you and Senator Hollings for your leadership in this whole area of competition.

I concur, Mr. Chairman, in your opening statement and I would say that you were, in fact, unfortunately, the prophet a few months ago with regard to what was going to happen in the airline industry. As you and this Committee very well know, a vibrant domestic aviation industry is essential to our nation's economy, and vigorous competition is required to ensure that it remains healthy. Right now, though, I fear that competition in the aviation industry is at risk.

If the mergers among United, US Airways, American Airlines, and TWA go forward as proposed, other major carriers likely will be forced to merge in order to remain viable competitors. Such consolidation could leave us with three, maybe four, megacarriers, each with extensive national networks that would make it very difficult for regional and startup carriers to compete.

Mr. Chairman, as we have learned through experience, when airlines are able to dominate a hub city they are likely to raise prices in that market, and therefore consumers can expect more of the same if several airlines are able to dominate large sections of our entire country.

Additionally, Mr. Chairman, I believe the nation as a whole would be at risk if we were to be forced to rely upon only a few megacarriers, as you say, three, maybe four, for the bulk of our air transportation needs. Mr. Chairman, we already have seen the terrible congestion and delays that passengers face when one of the major airlines has labor difficulties. I shudder to think of the impact on the flying public if a merged United-US Airways should ever face a work stoppage or other labor problems.

Before such a significant competition shift is allowed, Mr. Chairman, I believe we must examine thoroughly each of the related transactions to ensure that competition and consumers will not be harmed. That responsibility, of course, rests with the Justice Department and the Department of Transportation. But the Congress does and must play a role. To that extent, I believe that this Committee, as well as the Judiciary Committee, must examine these issues.

Accordingly, as Chairman of the Judiciary Committee's Antitrust Subcommittee, Ranking Minority Member Kohl and I have scheduled a hearing next Wednesday to examine the competitive impact of the proposed airline mergers. Based on what we have learned so far, it does not appear that these deals are good for the domestic aviation market nor for the American flying public as a whole. Instead, Mr. Chairman, it appears that the results of this consolidation will be to improve the fortunes of one or two giant airlines at the expense of the American consumer.

For that reason, a number of members of the Judiciary Committee have signed a letter to the Justice Department asking the Department to take special care to examine these proposed mergers in the aviation industry and focus specifically on the impact of such consolidation on passengers. With your permission, Mr. Chairman, I would like to offer that letter as a part of the record at this time.

The CHAIRMAN. Without objection.

[The material referred to follows:]

February 1, 2001

Hon. JOHN NANNES,
Acting Assistant Attorney General for Antitrust,
United States Department of Justice,
Washington, DC.

Dear Mr. Nannes:

We write to you to express our shared concern regarding increasing consolidation in the domestic aviation market. As you know, the airline industry plays a vital role in the American economy, and vigorous competition must be maintained to protect consumers and ensure a healthy aviation system. The proposed transactions among United Airlines, US Airways and American Airlines raise serious competition concerns, and we urge you to closely examine these transactions to ensure that consumers are protected.

When United Airlines and US Airways announced their merger, many expressed concern that such a merger would cause a chain-reaction of other mergers that would lead to massive consolidation within the industry. The recent deal announced by American Airlines makes it clear that such concerns are justified. If all pending transactions are approved, American Airlines and United Airlines will grow significantly larger than their nearest competitors. forcing the remaining "large" airlines to expand via merger in order to compete effectively. We fear that the long term effects of such consolidation will be a decrease in competition, higher fares, and less focus on passenger satisfaction. In an industry already struggling with customer service, we cannot afford any further deterioration in this area.

Accordingly, we ask that you continue to examine the mergers pending in the aviation industry, with a special focus on the impact that such consolidation will have on competition and consumers.

Sincerely,

MIKE DEWINE,
HERB KOHL,
PATRICK LEAHY,
CHARLES SCHUMER,
CHUCK GRASSLEY,
RUSS FEINGOLD,
ARLEN SPECTER,
STROM THURMOND,

Senator DEWINE. Again, Mr. Chairman, I want to thank you for the opportunity to testify on this important issue. I look forward to working with all the Members of the Commerce Committee as we examine these mergers and as we try to determine how best to protect the interests of consumers and of competition in our domestic aviation market.

I thank the chair.

The CHAIRMAN. Thank you, Senator DeWine, and we look forward to working with you and your Subcommittee on this issue. Obviously from your statement, we are in agreement that there is a lot more to come on this issue.

Governor Holden, welcome to the Committee. Congratulations on your recent election and we appreciate you taking time to be with us this morning.

STATEMENT OF HON. BOB HOLDEN, GOVERNOR, STATE OF MISSOURI

Governor Holden: Thank you very much, Mr. Chairman.

Let me first of all just second our Senator's comments. I appreciate those remarks very much, Senator Bond.

Senator Hollings, other Members of the Committee: My name is Bob Holden, Governor of Missouri. I appreciate the opportunity to speak to you today regarding the proposed buyout of TWA by American Airlines on behalf of the State of Missouri. I am particularly pleased to see that Jean Carnahan, the new Senator from Missouri, is a Member of this Committee, and I look forward to working with her also on this effort, because I know that she and Senator Bond recognize, as I do, that this consolidation is critical if a healthy Missouri economy is to survive.

I share this Committee's conviction that competition must be fostered if the best interests of our consumers are to be served. I would respectfully submit that an American-TWA merger is fundamentally different than some of the other airline consolidations that have been considered. The primary difference is that in this case TWA cannot be saved without American's help. To our knowledge, American's proposal is the only offer, the only offer, that will allow Missouri to enjoy the same comprehensive airline service and economic benefits that TWA has provided in the past, and Senator Bond gave a rich history of that effort.

If TWA dies, the loss of this major employer would not only devastate Missouri's economy, but produce negative ripples throughout the world economy as well. TWA employs more than 12,000 Missourians at wages exceeding $604 million. Its flight and corporate headquarters in St. Louis, with 350 flights a day all over the world, make Lambert Airport an international transportation hub. Its Kansas City overhaul base and the administrative center, as well as ten daily flights connecting Kansas City and St. Louis, make TWA a major employment force in the area and a key transportation link within our state.

Yet, until American came forward, the only viable option for TWA was bankruptcy and the piecemeal sale of its assets. If this were to occur, Missouri would not only lose the jobs and transportation benefits created by TWA, but also the numerous other jobs interrelated to the airline industry. We believe that if this merger were prevented, Missouri would lose approximately 33,000 jobs and $876 million in annual wages, a devastating blow to our state's economic future.

Without the infusion of American's capital that has taken place, TWA would not be flying today as I speak to you. American has given us every assurance that its operations will ensure the continued employment of our citizens and the accessibility of airline travel that is so important to our economy. In fact, American envisions an enhanced future for TWA employees and this important Missouri transportation system.

As a public official, I join you in my concern for what the impact of increased consolidation in the aviation industry might mean for our country's future. However, I am far more concerned about the economic destruction, especially the loss of jobs, that would be wreaked on the State of Missouri if this acquisition does not take place.

Mr. Chairman, I hope that you and the other Members of the Committee will understand the differences between American's rescue of TWA and the other instances of airline consolidation. It is very, very different. I hope you will support this acquisition. Missouri's future will be dramatically affected by the decision that is made on this issue.

For the record, Mr. Chairman, I am also submitting statements from St. Louis Mayor Clarence Harmon [not provided], Lambert Airport Director Leonard Griggs [see Appendix], St. Louis County Executive Buzz Westfall [not provided], St. Louis Executive Dick Fleming of the RCGA [see Appendix], and Richard Bidwell of the St. Louis Visitors and Convention Bureau [see Appendix]. These people along with many others are very, very concerned about what happens with the American-TWA acquisition. This will truly have a significant impact on the State of Missouri.

I again want to say I applaud Senator Bond for his efforts on this issue that is so important for Missouri. We appreciate it very, very much.

[The prepared statement of Governor Holden follows:]

PREPARED STATEMENT OF HON. BOB HOLDEN, GOVERNOR, STATE OF MISSOURI

Chairman McCain, Ranking Member Hollings and Members of the Committee, on behalf of the State of Missouri, I appreciate the opportunity to speak to you today regarding the proposed acquisition of TWA by American Airlines.

I'm particularly happy to see my friend Senator Jean Carnahan, former First Lady of Missouri, here today on the Committee. I know she shares my concerns about the effects the failure of this proposed acquisition will have on the people of our state. Numerous jobs and the competitiveness of Missouri hang in the balance.

Mr. Chairman, I know that there is a great deal of concern among your colleagues on both sides of the aisle, and in the previous Congress, regarding consolidation in the airline industry. The industry was deregulated to promote competition, and that action met with some measure of success. We have new airlines such as Southwest Airlines, Midwest Express and America West. For some routes, the competition led to better service and decreased fares. The other end of the spectrum, however, is the concern that a few airlines will become so dominant as to avoid true competition. This has been the focus of this Committee's attention in recent years. At the core of all of this is the common concern for the people—the consumers of airline services.

Mr. Chairman, I share with you and the Members of this Committee the desire for better service and lower fares for our citizens, which are achieved through open competition, and I appreciate this Committee's role to ensure that open competition continues. The balance of interests that must be struck in any proposed merger or acquisition is no small feat, and I do not suggest that I am an expert on airline mergers or can explain to this Committee the details of the numerous effects of this proposed acquisition as it affects the various airports nationwide and internationally. What I am here to affirm is that the State of Missouri is excited about the probable results of this acquisition. We are also concerned about the effects a failure of this acquisition will have on the state of Missouri.

TWA and its corporate predecessors have a long history with the state of Missouri. TWA has had a presence in St. Louis since the 1920s. After deregulation, Lambert Airfield became a hub for TWA and has been ever since—a period of a quarter of a century. TWA currently has nearly 8,000 jobs tied to the technical operations of the airline in St. Louis, with annual wages of over 390 million dollars.

The corporate headquarters were relocated to St. Louis, Missouri, in 1994. Currently, TWA employs nearly 2,000 people in its corporate and administrative offices in St. Louis and Kansas City, with annual wages of 77 million dollars.

The maintenance and overhaul base in Kansas City has existed for over 40 years. It actually was the first entity to be located where Kansas City International Airport is now located. The facility currently employs over 2,600 Missourians with annual wages exceeding 132 million dollars.

Mr. Chairman, TWA employs more than 12,000 Missourians at wages exceeding 604 million dollars. TWA offers 350 flights a day from St. Louis' Lambert Airport. The airline serves 83 cities around the world and 38 states, Mexico, Canada and the Caribbean. TWA's presence has been felt in Missouri and its recent financial difficulties have been felt as well. TWA filed for bankruptcy twice in the 1990s. State assistance was authorized in 1993 to help the financial condition of the company. We have been acutely aware of the company's ups and downs and would be devastated were the company's operations to simply fold.

At this juncture, TWA was facing a disturbing future as its only option—bankruptcy and piecemeal sale of its assets. Were this to happen, Missouri would lose not only the jobs directly created by TWA, but numerous other jobs due to the indirect effects of closing. Nearly 33,000 jobs and $876 million annually in wages would be lost, a devastating blow from which the state would not recover in the foreseeable future. Its closure would have produced negative ripples throughout the world economy.

The company was in dire straits and was forced to make a very difficult decision. American Airlines made an offer to acquire TWA. The choice lay between letting the venerable airline die quickly, which would have meant near certain economic chaos for Missouri's economy, or seeking a transfusion that would let it live on as a stronger entity. The acquisition was the best solution.

The deal struck between the parties, including the debtor in possession status, saves over 12,000 jobs in Missouri and ensures the continuation of hundreds of flights daily from the St. Louis hub serving the United States and beyond. Time is of the essence. If American had not infused capital into TWA, flights would not be taking place as we speak. If the company has to be dissolved and only its prime assets sold bit by bit, Missouri will be devastated. American's proposed solution is currently the only viable offer.

Through its ongoing infusion of operating capital and proposed acquisition of TWA, Missourians may no longer have the cherished moniker of "TWA" to refer to our longtime partner in the airline industry, but, more importantly, we will be ensured continued employment of our citizens and the accessibility of airline travel that is so important to the region's economy.

American has resuscitated everything that TWA provides to Missouri; we also envision that it will enhance the future of both the employees and the region's transportation system. American has reassured the state that the airline's hub will be maintained and most likely improved in the future. Lambert Airport is critical to Missouri's transportation system and economy. Lambert carries an economic impact of $5 billion on its region. Its maintenance and future expansion are vital to the region and state's efforts to take full advantage of future global economic opportunities in the new economy.

We need to recognize a fundamental difference between the American/TWA merger and some of the other airline consolidations that have been under consideration. The primary difference in the TWA/American deal is that TWA cannot be saved without help from American. Without American's help, TWA was going to die, with terrible consequences for the economy.

The current economic slowdown has caused the loss of companies such as Montgomery Ward's and numerous layoffs in companies across the state and the nation. The loss of a major employer such as TWA would be particularly devastating to Missouri's economy.

As a public official, I, too, am concerned about the impact of increased consolidation in the aviation industry. However, I am far more concerned about the economic damage, especially the loss of jobs, that would be inflicted on my state and the nation if this acquisition does not take place.

Mr. Chairman, I hope that you and the other Members of the Committee will understand the differences between America's resuscitation of TWA and the other instances of airline consolidation, and I hope that you will support this acquisition.

Mr. Chairman, I thank you once again for the opportunity to speak on behalf of this issue, which is of vital interest to our state and nation.

For the record, Mr. Chairman, I am submitting documents that will help to show the significance of this decision. In addition, I am submitting statements of support for the record from St. Louis Mayor Clarence Harmon and Lambert Airport Director Leonard Griggs; St. Louis County Executive Buzz Westfall; Richard Fleming, of the Regional Chamber and Growth Association; and Robert Bidell, of the St. Louis Visitors and Convention Bureau.

The CHAIRMAN. Thank you, Governor Holden.

Congressman Meeks, welcome.

STATEMENT OF HON. GREGORY W. MEEKS, U.S. REPRESENTATIVE FROM NEW YORK

Mr. MEEKS. Thank you, Mr. Chairman and Senator Hollings and the other distinguished Members of the Committee. I want to thank you for the opportunity to testify today.

Quite simply, I am here today because this issue has a profound significance for my district's current and future economic welfare. At a time when major corporations are reducing their workforce by the thousands and our economy continues to show signs of weakness, the bankruptcy court and the Justice Department have the opportunity to preserve thousands of jobs by immediately approving the acquisition of TWA's assets by American Airlines.

By doing so, it will preserve more than 4,000 jobs at John F. Kennedy International Airport, which lies in the heart of my Congressional district, and more than 20,000 jobs nationwide. Furthermore, this deal also provides the much needed financial stability of American Airlines' balance sheet to TWA's employees, creditors, and other stakeholders, who have been wandering in the financial desert since 1988.

As Missouri Senator Jean Carnahan commented last week, I too view this not as a merger proposal, but as a rescue mission for

TWA. Let me be very clear. Without American's intervention, TWA would have shut down around January 10th. A TWA shutdown would have meant not only thousands of employees out of work, but it would have resulted in the elimination of air service to communities in the Northeast and throughout the Midwest.

It is also important for you to recognize the economic impact of having an airline go out of business. My district still suffers from the devastating economic losses of Eastern Airlines and Pan American Airlines. In both cases the court allowed the airline's assets to be liquidated to the highest bidder. It resulted in the two airlines' competitors acquiring Eastern and Pan Am's most prized routes only, and resulted in thousands of permanent displaced workers, who in many cases were employed by one of the carriers for more than 30 years.

This action by the bankruptcy court left those Americans without a job and no benefits after a lifetime of service and dedication to Eastern or Pan Am. Clearly, we must not repeat that mistake.

As such, the proposed American-TWA transaction must be quickly resolved through the bankruptcy court and by the Justice Department to ensure the continued long-term employment of thousands of New York residents who either work for TWA or whose companies provide services for TWA. I ask you to recognize the immediate urgency of this situation and that it represents a truly exceptional circumstance.

This deal is about preserving jobs and the retirement security of TWA's retirees, thousands of jobs and thousands of retirees' benefits. Any delay in the review process of the American-TWA transaction only serves to harm TWA's employees and their families and jeopardize the air service now provided by TWA.

At this time I would also like to express my strong support for the DC Air transaction. The partnership DC Air has entered into with American Airlines gives DC Air the capacity to provide a higher level of service at a lower cost upon its initial operations that it would otherwise have not been able to provide. By doing so, it gives Mr. Bob Johnson and DC Air the opportunity to succeed as a new entrant in the very competitive airline industry.

The strategic partnership between DC Air and American Airlines addresses the competition issues, and provides an infusion of capital from the 49 percent stake being purchased by American and DC Air and ensures that DC Air will have the airplanes and crews available to serve its 45 communities from its inception.

The DC Air and American Airlines partnership enables DC Air to move from a virtual airline, which it must remain until the United-US Airways merger is approved, to a fully operational airline serving some 45 communities from Washington National Airport overnight. It ensures that the commitment which DC Air has made to uninterrupted service to these communities will be kept and that DC Air will be a strong competitor to United Airlines at National Airport.

The DC Air-American Airlines partnership ensures the initial success of DC Air as an independent entity with a lower cost structure which can now be translated into lower fares for the consumers which it will serve on the 45 routes by DC Air.

Mr. Chairman, let me conclude by thanking you for the opportunity to testify, and I hope that this distinguished Committee sees the many public interest benefits of DC Air as well as the American-TWA transaction. Thank you.

[The prepared statement of Representative Meeks follows:]

PREPARED STATEMENT OF HON. GREGORY W. MEEKS, U.S. REPRESENTATIVE FROM NEW YORK

Chairman McCain, Ranking Member Hollings, and other distinguished Members of the Committee, thank you for the opportunity to testify today. Quite simply, I am here today because this issue has a profound significance for my district's current and future economic welfare.

At a time when major corporations are reducing their workforce by the thousands and our economy continues to show signs of weakness, the bankruptcy court and Justice Department have the opportunity to preserve thousands of jobs by immediately approving the acquisition of TWA's assets by American Airlines. By doing this, it will preserve more than 4,000 jobs at John F. Kennedy International Airport, which lies in the center of my congressional district, and more than 20,000 jobs nationwide. Furthermore, this deal also provides the much-needed financial stability of American Airlines' balance sheet to TWA's employees, creditors and other stakeholders who have been wandering in the financial desert since 1988.

As Missouri Senator Jean Carnahan commented last week, I too view American Airlines' proposal as a rescue mission for TWA. Let me be very clear: without American's intervention, TWA would have shut down around January 10th. A TWA shut down would have meant not only the thousands of employees out of work, but it would have resulted in the elimination of air service to communities in the northeast and throughout the midwest.

It is also important for you to recognize the economic impact of having an airline go out of business. My district still suffers from the devastating economic losses of Eastern Airlines and Pan American Airways. In both cases, the court allowed the airlines' assets to be liquidated to the highest bidder. It resulted in the two airlines' competitors acquiring Eastern and Pan Am's most prized routes. However, it also resulted in thousands of permanent displaced workers, who, in many cases, were employed by one of the carriers for more than 30 years. This action by the bankruptcy court left those Americans without any job and no benefits after a lifetime of service and dedication to Eastern or Pan Am. Clearly, we must not repeat that mistake again.

As such, the proposed American/TWA transaction must be quickly resolved through the bankruptcy court and by the Justice Department to ensure the continued, long-term employment of thousands of New York residents who either work for TWA or whose companies provide services for TWA. I ask you to recognize the immediate urgency of this situation and that it represents, a truly exceptional circumstance. This deal is about preserving jobs and the retirement security of TWA's retirees—thousands of jobs and thousands of retirees' benefits. Any delay in the review process of the American/TWA transaction only serves to harm TWA's employees and their families, and jeopardize the air service now provided by TWA.

I would also like to express my strong support for the DC Air transaction. The partnership which DC Air has entered into with American Airlines gives DC Air the capacity to provide a higher level of service at a lower cost upon its initial operations than it would otherwise have been able to provide. By doing so, it gives Bob Johnson and DC Air the opportunity to succeed as a new entrant in the very competitive airline industry.

The strategic partnership between DC Air and American Airlines addresses the competition issues, provides an infusion of capital from the 49 percent stake being purchased by American in DC Air, and ensures that DC Air will have the airplanes and crews available to serve its 45 communities from its inception.

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The DC Air/American Airlines partnership ensures the initial success of DC Air as an independent entity with a lower cost structure which can now be translated into lower fares for the consumers which will be served on the 45 routes by DC Air.

Mr. Chairman, let me conclude by again thanking you for the opportunity to testify. I hope that this distinguished Committee sees the many public interest benefits of DC Air as well as the American/TWA transaction.

The CHAIRMAN. Thank you very much, Congressman Meeks.

I want to thank all of you for testifying this morning. We appreciate you taking the time from your busy schedule. Governor, we especially appreciate your presence here as well. Thank you very much.

Our next panel is: Mr. Donald Carty, who is Chairman, President, and CEO of American Airlines; Mr. William F. Compton, President and CEO of Trans World Airlines; Mr. Robert L. Johnson, who is the Chairman and CEO of DC Air; Mr. Joe Leonard, who is the Chairman and CEO of AirTran; Professor Michael E. Levine, Adjunct Professor of Law at the Harvard Law School; and Ms. JayEtta Z. Hecker, Director of Physical Infrastructure Issues at the U.S. General Accounting Office.

As the witnesses are taking their seats, I would like to conduct a little Committee business and ask unanimous consent for the rules of the Committee, which Senator Hollings and I have agreed on, including an agreement that half of the witnesses will be chosen by either side, as well as half the staffing, as well as half the budget. Is there objection?

[No response.]

The CHAIRMAN. If not, the rules of the Committee are adopted. Did you want to say anything?

Senator HOLLINGS. No. That is good. Thank you.

The CHAIRMAN. Mr. Carty, it is very rare that you have been described as a white knight, a shining knight on a white horse.

STATEMENT OF DONALD CARTY, CHAIRMAN, PRESIDENT, AND CEO, AMERICAN AIRLINES

Mr. CARTY. My children do frequently, Senator.

The CHAIRMAN. Quite remarkably. I guess we are deeply honored to have you here. Thank you and welcome back before the Committee, Mr. Carty.

Mr. CARTY. Thank you, Chairman McCain, Senator Hollings and other Members of the Committee. I appreciate the opportunity to appear again before this Committee and testify on consolidation in the airline industry.

Ever since United Airlines proposed acquiring US Airways last May, airline consolidation has clearly been on the Committee's radar screen, and appropriately so. Members of this Committee and industry observers have expressed strong concerns about the potential impact of United's proposal. Likewise, many have warned that its approval would inevitably spark more mergers and more acquisitions.

As you may recall, I testified before this Committee last September that United's proposed merger with US Airways had triggered us at American to think long and hard about a defensive response. That examination, of course, resulted in our announcement last month of an agreement that directly addresses many of our concerns about the size and the scope of the United-US Airways merger while I think positioning American as a much more vigorous competitor in the Northeast.

Now, coincidentally—and it was largely coincidentally—an opportunity arose for us to enter into a completely separate and unrelated transaction. Coincident with TWA's bankruptcy filing on January 9th, we agreed, as has already been said this morning, to acquire substantially all of TWA's assets and provide it $200 million in financing so that the airline could continue to operate while in bankruptcy.

Now, the immediacy of TWA's situation, as well as the carrier's significantly smaller size, clearly I think dictates that this transaction be treated differently and swiftly. Let me begin, however, by addressing the broader question of airline consolidation. In an increasingly globalized business such as ours, network size and scope are very important competitive issues for airlines. The original United-US Airways proposal presented a very serious competitive challenge. Had its initial proposal been approved, United would have become 50 percent bigger than its nearest competitor, namely us of course.

As you might imagine, for a company like ours that is determined to create a network that is second to none, this clearly got our attention. The ultimate size of United's route network was not the only cause of concern. High market concentration on routes to and from the nation's capital led United and US Airways to propose creating a new entrant at Reagan National Airport named DC Air. While I tip my hat to both carriers for being able to persuade such an accomplished businessman as Bob Johnson to join this crazy industry, I think that the relationship originally articulated and envisioned between United and DC Air caused many of us to be somewhat skeptical.

The potential effect on competition in the Northeast and on routes between United's hubs and US Airways's hubs was also problematic. American has a relatively small share of the key business of routes between Boston, New York, and Washington, and our fear was that the proposed merger would entrench United, complete with its new vastly larger transcontinental network, in an effective duopoly with Delta in those shuttle markets.

But of course, as everyone knows now, in the closing months of last year I think it became apparent that the original United-US Airways proposal simply would not stand. That prompted American—and I might add, a number of our other competitors—to enter into discussions with the merger parties regarding proposals of asset sales. As everyone now knows, in early January we agreed to acquire from US Airways 14 gates, 36 slots, 66 owned aircraft, and an additional 20 leased aircraft, as well as the gates and slots necessary for us to operate half of what is today the US Airways shuttle.

In addition, to introduce immediate new competition on United Airways hub to hub routes, we agreed to guarantee competition on five such routes. As for DC Air, we agreed to take a 49 percent stake in the carrier and entertain an exclusive marketing arrangement with it in which DC Air will participate in American's frequent flyer program and we will provide DC Air with some 11 aircraft worth of flying.

Now, taken together, we believe these transactions relieve many of the competitive issues associated with imbalance in the Northeast. They are going to increase competition by making DC Air a real competitor to United with a significant independent backing, while affording us, American, for the first time a significant presence in Washington, D.C., and the Northeast.

Our expanded presence throughout the upper East Coast is going to ensure there are at least three major carriers of comparable size on the shuttle routes and at least two competitors on the hub to hub routes. Passengers traveling along the East Coast are also going to benefit by our establishing another source of connecting service to compete with the service offered by United, Delta, Continental, and a number of other East Coast competitors.

Now, obviously we have given the Justice Department and Congress a lot to digest, and American looks forward to working both with Justice and with this Committee as you attempt to determine whether what we have put on the table sufficiently remedies the United-US Airways merger and ultimately benefits the flying public.

On a more personal note, regardless of Justice's disposition of the transaction before it, I must say that I have gotten to know Bob Johnson over these past few months. He is a take-charge executive who knows how to provide consumers a service. He has proven that. Let there be no mistake, Bob Johnson and his team are going to run DC Air. He is going to be the majority owner and he will make the decisions.

We will obviously be his marketing partner and we are going to work very closely together to add value to our respective networks. DC Air is going to be a very valuable addition to our industry and bring to it, as has already been said, one of the first minority-owned airlines. We at American are very proud to be affiliated with it.

Now let me turn to TWA, a story of a beleaguered airline that, after 12 consecutive years of heavy losses and three bankruptcies, has, in spite of valiant efforts by my associate Bill Compton and his team, simply run out of money, time, and options. Carl Icahn has stripped this company over a period of years, selling assets to pay the bills. Going into this winter, with the price of fuel soaring, TWA had nothing left to sell or mortgage that was not already encumbered.

It also had a debt of $100 million coming due on January 15th. Unable to secure or justify additional financing from traditional sources, with no one willing to purchase the airline, TWA in early January faced the very real likelihood that it would have to shut down and liquidate.

Now, as has already been said, at that point we stepped in to provide, when no one else would, the $200 million TWA had to have to keep operating. We are proposing to acquire substantially all of TWA's assets, to hire all of TWA's employees, and to continue a hub operation in St. Louis. Now, obviously this transaction, which excludes certain TWA contracts such as Mr. Icahn's deal, is going to be contingent on the bankruptcy court's approval.

In closing, permit me to be very blunt. Time is of the essence with respect to TWA. The carrier has already consumed more than three-quarters of the cash provided on January 11th. We at American cannot commit our shareholders' money to keep TWA afloat indefinitely. There is simply not enough collateral for further debtor-in-possession financing. Also, I fear—and I think Bill shares this fear—that uncertainty is only going to serve to accelerate TWA's collapse because, as inevitably happens, customers and travel agents eventually book away from uncertainty.

As for the Justice Department review of the transaction, I think it is fairly evident that there is a failed firm here, which in itself should serve to expedite that review process. Even so, the transaction gives rise to very few competition issues. Indeed, the market share of this one-time giant of the skies has now fallen to less than 4 percent in the year 2000.

The bottom line is that TWA's situation represents a truly unique and a truly exceptional circumstance. Indeed, our acquisition of its assets is not contingent on the approval of any other deal. As such, it is truly a stretch of the imagination to believe that the American-TWA transaction could in any way trigger the merger of far larger airlines. Instead, in this instance what is before this Committee is our taking on a financial risk that no other airline was willing to take and commitments to the 20,000 TWA employees and their families that no one else would make.

Mr. Chairman, that concludes my statement and I would be happy to answer any questions at the appropriate time.

[The prepared statement of Mr. Carty follows:]

PREPARED STATEMENT OF DONALD CARTY, CHAIRMAN, PRESIDENT, AND CEO, AMERICAN AIRLINES

Good morning. Thank you for the opportunity to appear again before this Committee and testify on consolidation in the airline industry. Ever since United Airlines proposed acquiring US Airways last May, airline consolidation has clearly been on this Committee's radar screen. And rightly so.

Members of this Committee and industry observers have expressed strong concerns about the potential impact of United's proposal. Likewise, many have warned that its approval would inevitably spark more mergers or acquisitions. As you may recall, I testified before this Committee last September that United's proposed merger with US Airways had triggered us at American Airlines to think long and hard about a defensive response. That examination resulted in our announcement last month of an agreement that directly addresses many of our concerns about the size and scope of the United/US Airways merger while positioning American as a much more vigorous competitor in the Northeast.

Coincidentally, an opportunity arose for us to enter into a completely separate and unrelated transaction. Quite simply, TWA's continuing downward financial spiral had finally reached a point of no return, threatening the jobs of its 20,000 employees and air service to communities throughout the nation's heartland. With only $20 million in the bank and needing $40 million to meet its obligations necessary for operating a normal schedule, TWA filed bankruptcy on January 9. We agreed to acquire substantially all of TWA's assets and have provided it $200 million in financing so that the airline can continue to fly during bankruptcy. As I will discuss in more detail later, the immediacy of TWA's situation as well as the carrier's significantly smaller size clearly dictates that this transaction be treated swiftly.

Let me begin, however, by addressing the broader question of airline consolidation. In an increasingly globalized business such as ours, competition will suffer if one network is allowed to dwarf all other networks. From a customer perspective, the benefits of a much broader network are clear. Our customers—both leisure and business travelers—increasingly expect their airline of choice to be able to take them everywhere they want to go. Accordingly, if one airline is able to grow its route network significantly larger than its competitors, that airline would have a competitive advantage.

The original United/US Airways proposal presented just such a scenario. Had its initial proposal been approved, United would have become 50 percent bigger than its nearest competitor, namely us. As you might imagine, for a company like ours that is determined to create a domestic and international network that is second to none, this got our attention. For air travelers, the unbalanced landscape caused by the lack of one or more competing networks of similar size and breadth would have surely led, I believe, to an eventual reduction in overall competition.

The ultimate size of United's route network was not the only cause for concern. As we all know, high market concentration on routes to and from the nation's capital led United and US Airways to propose creating a new entrant at Reagan National Airport named DC Air. While I tip my hat to both carriers for being able to persuade such an accomplished businessman as Robert Johnson to get mixed up in our industry—where margins are thin and headaches plenty—I think the relationship envisioned between United and DC Air caused most everyone, both inside government and out, to be somewhat skeptical. Simply put, it was hard to see any competitive benefit coming from the transaction given that DC Air's aircraft, flight crews, operational support, and management staff were mostly being supplied by either United or US Airways.

The potential effect on competition in the Northeast and on routes between United's hubs and US Airways' hubs was also problematic. American has a relatively small share of the key business routes between Boston, New York, and Washington, D.C. Our fear was that the proposed merger would entrench United, complete with its new, vastly larger transcontinental network, in an effective duopoloy with Delta in these shuttle markets, an outcome that rightly alarmed outside observers as well.

In the closing months of last year, it became apparent that the original United/USAirways proposal would not stand. This prompted American—and a number of other competitors—to enter into discussions with the merger parties regarding proposals of asset sales.

In early January, we agreed to acquire certain key strategic assets from US Airways and to acquire a substantial stake in DC Air—both contingent upon the reconstituted United/US Airways merger receiving regulatory approval. In a nutshell, we would acquire from US Airways 14 gates, 36 slots, 66 owned aircraft and an additional 20 leased aircraft, as well as the gates and slots necessary for us to operate half of the US Airways Shuttle. In addition, to introduce immediate new competition on United/US Airways hub-to-hub routes, we agreed to guarantee that the following routes would be served by at least two roundtrips a day for the next 10 years: Philadelphia-Los Angeles, Philadelphia-San Jose, Philadelphia-Denver, Charlotte-Chicago, and Washington, DC.-Pittsburgh.

As for DC Air, we agreed to take a 49 percent stake in the carrier and enter an exclusive marketing arrangement with it in which DC Air will participate in American's frequent flyer program. We will also provide DC Air with 11 100-seat Fokker 100 aircraft in an arrangement by which American Airlines personnel will be flying and maintaining AA aircraft marketed as DC Air service. American will also have the right of first refusal on the acquisition of the remaining 51 percent of DC Air.

Taken together, we believe these transactions relieve the competitive imbalance in the Northeast. They will also increase competition by making DC Air a real competitor with significant independent backing while affording us, for the first time, a significant presence in Washington, D.C. and the Northeast. American, for example, now accounts for roughly 13 percent of passenger boardings at Reagan National and far less than that at Washington Dulles and BWI. As in the Washington area, our expanded presence throughout the upper East Coast will ensure that there are at least three major competitors of comparable size on the Shuttle routes and at least two competitors on the hub-to-hub routes. And, passengers travelling along the East Coast will also benefit by our establishing another source of connecting service to compete with the service offered by United, Delta, Continental and other East Coast competitors.

Obviously, we have given the Justice Department and the Congress a lot to digest. American looks forward to working with both Justice and this Committee as you attempt to determine whether what we have put on the table sufficiently remedies the United/US Airways merger and, ultimately benefits the flying public.

On a more personal note, regardless of Justice's disposition of the transactions before it, I must say that I have gotten to know Robert Johnson over these past few months and am most impressed. He is a take-charge executive who knows how to provide consumers a service, and quite frankly, how to make money. Let there be no mistake, Robert Johnson and his team will run DC Air. He will be the majority owner and he will make the decisions. He has already begun recruiting a seasoned management team. American will be his marketing partner, and we will work closely together to add value to our respective networks. DC Air will be a valuable addition to our industry and bring to it the first minority-owned airline. I know that I speak for each and every one of American's 103,000 employees when I say that it has taken our industry far too long to reach this milestone and that we at American are proud to be affiliated with it.

As for the impact of American's entry into this equation, Jim Wilding, the president of the Metropolitan Washington Airports Authority, was recently quoted as being highly enthusiastic about the vigorous competition that American's affiliation with DC Air will bring to the Washington market in comparison with the original proposal. In Mr. Wilding's words: "If American and United are anything, they're competitors. They're like the cobra and the mongoose wherever they go."

Now let me turn to TWA—a storied but beleaguered airline that after 12 consecutive years of heavy losses and 3 bankruptcies has, in spite of valiant efforts by Bill Compton and his team, simply run out of money, time, and options. Carl Icahn has stripped this company over a period of years, selling assets, such as the prized route rights to London's Heathrow Airport, just to pay the bills. Going into this winter, typically the leanest months in the airline business, with the price of fuel soaring, TWA had nothing left to sell or mortgage that wasn't already encumbered. It also had a debt of $100 million coming due on January 15. Unable to secure or justify additional financing from traditional sources and with no one willing to purchase the airline, TWA in early January faced the very real likelihood that it would have to shut down and liquidate.

From time to time, we at American had looked at TWA as a possible merger candidate. Indeed, its centrally located St. Louis hub provides a nice complement to our operations at capacity constrained Chicago O'Hare. In addition, TWA's current management team had—in the face of some formidable obstacles—done a very good job of improving the airline's operation, and in particular, of modernizing its fleet. Unfortunately, very high ownership costs on TWA's new fleet and an unusual arrangement that allows an entity owned by Carl Icahn to sell TWA's ticket inventory at a substantial discount, made a potential AA/TWA merger a non-starter.

TWA's bankruptcy filing and looming collapse three weeks ago, however, presented a far different set of circumstances. We stepped in to provide—when no one else would—the cash TWA had to have to keep operating. We are proposing to acquire substantially all of TWA's assets, to hire all of TWA's employees and to continue a hub operation in St. Louis. Obviously, this transaction, which excludes certain TWA contracts such as Mr. Icahn's deal, is contingent on bankruptcy court approval.

Senator Carnahan, let me say to you in particular that we look forward to adding TWA's 20,000 employees to the American Airlines family. We are keenly aware of TWA's illustrious history and know that were it not for the hard work and great performance of the people throughout TWA, they would not be the perfect fit for American that we believe they are. We also recognize what a good corporate citizen TWA has been in the state of Missouri and I can assure you that our company will be as well.

In closing, permit me to be blunt. Time is of the essence with regard to TWA. We at American cannot commit our shareholders' money to keep TWA afloat indefinitely. There is simply not enough collateral for debtor in possession financing. Also, I fear, uncertainty will only serve to accelerate TWA's collapse as travel agents will likely book away from TWA, as was the case with the demise of Eastern Air Lines a decade ago. Similarly, consumer uncertainty will eventually cause travelers to not advance book flights on TWA, effectively shutting off the airline's already severely limited cash flow.

As for the Justice Department review of this transaction, I think it is fairly evident that there is a failed firm here, which in itself should serve to expedite the review process. Even so, the transaction gives rise to very few competition issues. Indeed, the market share of this one-time giant of the skies has now fallen to only 3.9 percent in 2000. Finally, even if TWA were not failing and therefore unable to compete on a going-forward basis, there are only two hub-to-hub routes where American and TWA both offer non-stop service. In the case of St. Louis-Chicago, for example, Southwest Airlines, which has 12 gates at St. Louis Lambert, provides 15 daily nonstop roundtrips between St. Louis and Chicago Midway, while United provides 4 daily nonstops between St. Louis and Chicago O'Hare.

The bottom line is that TWA's situation presents a truly unique and exceptional circumstance. Indeed, our acquisition of its assets is not contingent on approval of the other deals. As such, it is truly a stretch of the imagination to believe that the American/TWA transaction could in any way trigger the merger of far larger airlines. Instead, what is before you is our taking on a financial risk that no other airline was willing to take and commitments to the 20,000 TWA employees and their families that no one else would make.

Mr. Chairman, that concludes my statement. I would be happy to answer any questions you or the Members of this Committee may have.

The CHAIRMAN. Thank you, Mr. Carty.

Mr. Compton, welcome.

STATEMENT OF WILLIAM F. COMPTON, PRESIDENT AND CEO, TRANS WORLD AIRLINES

Mr. COMPTON. Thank you, Chairman McCain and Ranking Member Hollings and other Members of this distinguished Committee. On behalf of TWA's 20,000 employees, I thank you for the opportunity to testify here today. I appreciate the chance to explain why our decision to pursue an asset purchase agreement with American Airlines should be approved and why this transaction is a good global solution for TWA's customers, our employees, our retirees, and other stakeholders, as well as the communities served by both carriers.

I would like to begin by giving you my personal perspective on TWA on why in my view the proposed transaction is the only comprehensive solution that adequately serves the consumers in light of the harsh realities facing TWA, its employees, and retirees. Since the late 1960's when I became a pilot with TWA, the airline industry and the economy have changed dramatically. It has been an uphill battle for TWA, particularly over the last 15 years, simply to survive.

In 1985 TWA, during the height of the Wall Street-driven mergers and acquisitions, was acquired by Carl Icahn. Subsequently, TWA was stripped of its most valuable assets. Through the efforts and commitment of its employees, TWA eventually was able to secure a change in corporate ownership. At that point, however, TWA was saddled with enormous debt, an aging fleet, a pension fund that had been deemed to be seriously underfunded, and the loss through sale of many of its most valuable routes.

The fact that TWA survived in those circumstances is due to the sheer dedication of its employees. They gave concessions and survived not one, but two bankruptcies, to ensure the continuation of the airline to the present time. In fact, notwithstanding the financial predicament, TWA has made a remarkable operational turnaround over the last 4 years. TWA has been ranked at or near the No. 1 spot for on-time performance since 1997. In 1998 and 1999 customers voted us the winner of the J.D. Power award for customer satisfaction. In 2000 we finished second amongst all airline in both J.D. Power award categories.

We replaced most of our entire fleet, with the result that it is now on average one of the more younger fleets in the airline industry. We made these improvements without huge capital outlays or marketing campaigns. We did it with dedication, professionalism, and pride—hallmarks of TWA throughout its 75 years.

But TWA's financial predicament continues and we can no longer afford to operate, let alone sustain these advances. Despite TWA's many accomplishments, profitability remained elusive. The events of the 1980's had made it virtually impossible to compete effectively. Due to its financial condition, TWA is still paying a premium for aircraft leases, paying nearly twice the industry average. The need to provide long-overdue wage increases for TWA employees and the recent staggering increases in the price of jet fuel have further drained TWA's reserves. TWA remains essentially a single-hub operation, putting us at a schedule disadvantage to the multiple-hub carriers.

Finally, this winter we ran out of time. In fact, by January 10th of 2001 TWA had cash on hand of only $20 million and needed significantly more than that just to operate through the next day. With our cash reserves nearly depleted and a major financial commitment to lenders coming due, our backs were squarely against the wall.

The financial crisis that hit TWA this winter did not materialize overnight. A year ago we could see problems looming on the horizon that culminated in our recent bankruptcy filing and we tried very hard to do something dramatic about it. We recognized that the viability of our airline was at stake and we went knocking on doors to find a solution. There is not an airline of any size in America that we did not approach. There is not an airline of any size in America that did not have the opportunity to step in and join with us.

No one was interested in TWA as a going concern. In my view, most recognized that they would benefit from TWA's demise and they were willing at best to stand back and watch it happen.

Only American Airlines saw fit this winter to come forward with a proposal that was not merely an offer to cherry-pick a prized asset here and a prized asset there. American proposed a comprehensive solution that will realize for our creditors the value of TWA as a going concern, that will preserve jobs for our employees and medical benefits for our retirees. It will maintain hub service in St. Louis and will safeguard TWA's major economic presence in additional communities around our system, most notably Kansas City, New York, and Los Angeles, where we employ thousands.

The transaction with American Airlines offers a comprehensive solution to the problems facing TWA. It addresses the varying needs of the TWA employees, retirees, creditors, and consumers and the communities served by TWA. This transaction offers protection for TWA's 20,000 employees and many thousands of our retirees and dependents. American has made a bedrock commitment to retain the vast majority of TWA employees and to absorb responsibility for TWA retirees' medical and dental insurance benefits. Not only does this speak volumes about American's integrity, it achieves TWA's goal of protecting its skilled and dedicated work force.

It is here that American is gaining TWA's greatest asset, its employees. American will find that it has acquired motivated employees who carry out their work with the highest level of quality and commitment.

The consumers and communities served by TWA also will be better served by the American transaction than by liquidation. Liquidation of TWA's assets without a commitment to maintaining TWA's jobs would result in vast reductions of service to many communities. Certainly, other carriers would benefit from such a reduction in competition, but consumers would pay the price.

The price to be paid in a TWA liquidation would be highest in our home State of Missouri and our hub city of St. Louis. In a court hearing last weekend, attorneys for the City of St. Louis stated that the economic contribution of Lambert-St. Louis International

Airport to the local economy is $8 billion per year. TWA and its regional alliance partners offer approximately 75 percent of the departures at Lambert. It is not difficult to envision the benefit of a continuation of this service under the auspices of American Airlines.

The communities would also be harmed by the liquidation alternative. TWA's 187 aircraft would cease to be in service. Air service to more than 100 communities would be negatively impacted. The result would be lower capacity, higher prices, less service for the traveling public, and a diminished business development capacity for dozens of communities.

An acquisition of TWA's assets as a total operation best serves to protect the traveling public and the communities that rely heavily on TWA. American has committed to retain the St. Louis hub operations. With additional aircraft from TWA in its system, American will be able to support TWA's route structure.

Several of our competitors are now suddenly saying, out of an apparent desire to avoid the enhancement of American, that TWA could be maintained as a stand-alone enterprise or its assets parceled out among various carriers to protect the interests of creditors. These claims, in addition to being disingenuous and self-serving, ignore the realities of the aircraft industry. They also disregard the needs of TWA consumers, employees, and retirees. In fact, they also do not represent the best options for TWA's largest creditors.

On balance, TWA believes that the American transaction presents the best protection for all TWA creditors. The American Airlines plan is the only global solution on the table and to us clearly offers the most benefit to the greatest number of TWA stakeholders.

As I look to the future of aviation, there are many chapters yet to be written. I believe, however, that the nature of TWA's final chapter will be viewed in the years to come as having provided major benefits to the aviation industry. Among the ranks of our current employees there are many young and talented people who have benefited from their apprenticeships under seasoned TWA veterans. They can take with them to American and to every corner of the aviation world knowledge and experience that is invaluable.

When I consider this possibility becoming a reality for so many of our workers through this transaction, I know that all of our efforts will have been worthwhile. Indeed, TWA's legacy, if not its grand name, will be carried forward by its people. Just as important, consumers will continue to see the same level of service, without the dislocation that would have otherwise occurred in a bankruptcy with a parceling out of assets. Indeed, this is the only way the public interest will be served in the long run.

Mr. Chairman, let me conclude by again thanking you for the opportunity to testify today. As I have said, we strongly believe this transaction should go forward and promptly. It is in the best interest of TWA's employees, retirees, creditors, consumers, and the communities served by both carriers.

I would be pleased to respond to questions. Thank you, Mr. Chairman.

[The prepared statement of Mr. Compton follows:]

PREPARED STATEMENT OF WILLIAM F. COMPTON, PRESIDENT AND CEO, TRANS WORLD AIRLINES

Chairman McCain, Ranking Member Hollings, and other Members of this distinguished Committee, on behalf of TWA's more than 20,000 employees, thank you for the opportunity to testify today. I appreciate the chance to explain why our decision to pursue an asset purchase agreement with American Airlines should be approved and why this transaction is a good global solution for TWA customers, employees, retirees, and other stakeholders as well as the communities served by both carriers.

In response to your letter of January 25th, Mr. Chairman, my statement will address the impact that the American acquisition of TWA will have on airline passengers, communities now served by TWA, TWA's creditors and TWA's employees and retirees. I would like to begin by giving you my personal perspective on TWA and why, in my view, the proposed transaction is the only comprehensive solution that adequately serves consumers in light of the harsh realities facing TWA, its employees and retirees.

I. How We Got Here

Since the late 1960s, when I became a pilot with TWA, the airline industry, and the economy have changed dramatically. It has been an uphill battle for TWA, particularly over the last 15 years, to simply survive. In 1985, TWA, during the height of Wall Street-driven mergers and acquisitions, was acquired by Carl Icahn. Subsequently, TWA was stripped of many of its most valuable assets.

Through the efforts and commitment of its employees, TWA eventually was able to secure a change in corporate ownership. At that point, however, TWA was saddled with enormous debt, an aging fleet, a pension fund that had been deemed to be seriously underfunded, and the loss through sale of many of its most valuable routes. The fact that TWA survived in those circumstances is due to the sheer dedication of its employees. They gave concessions and survived not one, but two, bankruptcies to ensure the continuation of the airline to the present time.

In fact, not withstanding its financial predicament, TWA has made a remarkable operational turnaround over the last four years. TWA has been ranked at or near the #1 spot for on-time arrivals since 1997. In 1998 and 1999, customers voted us the winner of the J.D. Power award for customer satisfaction. In 2000, we finished second among all of the airlines in both J.D. Power award categories. We replaced almost our entire fleet, with the result that it is now, on average, one of the youngest in the airline industry.

We made these improvements without huge capital outlays or marketing campaigns. We did it with dedication, professionalism, and pride—hallmarks of TWA throughout its 75 years. But, TWA's financial predicament continues and we can no longer afford to operate, let alone sustain these advances.

II. TWA's Many Successes Have Not Been Enough

Despite TWA's many accomplishments , profitability remained elusive. The events of the 1980s had made it virtually impossible to compete effectively. Due to its fragile financial condition, TWA is paying premium lease prices for its aircraft—almost twice the industry average. The need to provide long-overdue wage increases for TWA employees and the recent, staggering increases in the price of jet fuel have further drained TWA's reserves. TWA remains essentially a single hub operation, putting us at a schedule disadvantage to multiple hub carriers. Finally, this winter we ran out of time. In fact, by January 10, 2001, TWA had cash on hand of only $20 million and needed significantly more just to make it through the next day. With our cash reserves nearly depleted and a major financial commitment to lenders coming due, our backs were squarely against the wall.

The financial crisis that hit TWA this winter did not materialize overnight. A year ago we could see problems looming on the horizon that culminated in our recent bankruptcy filing, and we tried very hard to do something dramatic about it. We recognized that the viability of our airline was at stake and we went knocking on doors to find a solution. There is not an airline of any size in America that we did not approach. There is not an airline of any size in America that did not have an opportunity to step in and join with us. No one was interested in TWA as a going concern. In my view, most recognized that they would benefit from TWA's demise, and they were willing, at best, to stand back and watch it happen.

Only American Airlines saw fit this winter to come forward with a proposal that was not merely an offer to cherry-pick a prized asset here or there. American proposed a comprehensive solution that will realize for our creditors the value of TWA as a going concern. It will preserve jobs for our employees and medical benefits for our retirees. It will maintain hub service for St. Louis and will safeguard TWA's major economic presence in additional communities around our system—most notably Kansas City, New York and Los Angeles where we employ thousands.

III. American Airlines Transaction Offers Comprehensive Solution

The transaction proposed with American Airlines offers a comprehensive solution to the problems facing TWA. It addresses the varying needs of TWA employees, retirees, creditors, and consumers and the communities served by TWA.

This transaction offers protection for TWA's 20,000 employees and many thousands of our retirees and dependents. American has made a bedrock commitment to retain the vast majority of TWA employees and to absorb responsibility for TWA retirees' medical and dental insurance benefits. Not only does this speak volumes about American's integrity, it achieves TWA's goal of protecting its skilled and dedicated work force. It is here that American is gaining TWA's greatest asset—its employees. American will find that it has acquired motivated employees who carry out their work with the highest level of quality and commitment.

The consumers and the communities served by TWA also will be better served by the American transaction than by liquidation. Liquidation of TWA assets without a commitment to maintaining TWA jobs would result in vast reductions of service to many communities. Certainly other carriers would benefit from such a reduction in competition, but consumers would pay the price.

The price to be paid in a TWA liquidation would be highest in our home state of Missouri and our hub city St. Louis. In a court hearing last weekend, attorneys for the City of St. Louis stated that the economic contribution of Lambert-St. Louis International Airport to the local economy is $8 billion a year. TWA and its regional airline partners offer approximately 75 percent of the departures from Lambert. It is not difficult to envision the benefit of a continuation of this service under the auspices of American Airlines (or, for that matter, any other carrier that is willing to come forward in the auction process and commit to an acquisition of the TWA operation).

Other communities also would be harmed by the liquidation alternative. TWA's 187 aircraft could cease to be in service. Air service to more than 100 communities would be negatively impacted. The result could be lower capacity, higher prices, and less service for the traveling public and a diminished business development capacity for dozens of communities.

An acquisition of TWA assets as a total operation best serves to protect the traveling public and the communities that rely heavily on TWA. American has committed to retain the St. Louis hub operations. With additional aircraft from TWA in its system, American will be able to support TWA's route structure.

Several of our competitors are now suddenly saying, out of an apparent desire to avoid the enhancement of American, that TWA could be maintained as a standalone enterprise or its assets parceled out among various carriers to "protect the interest of the creditors." These claims, in addition to being disingenuous and self-serving, ignore the realities of the airline industry. They also disregard the needs of TWA consumers, employees and retirees. In fact, they also do not present the best options for TWA's largest creditors.

On balance, TWA believes that the American transaction presents the best protection for all TWA creditors. At present the offer from American is the only offer for the acquisition of TWA's assets actually on the table. Proposals put forth by others in the bankruptcy court will be evaluated and given serious consideration if and when they come forward. Our assets will be sold through a bankruptcy auction process and we remain open to higher and better offers. But, so far, the American Airlines plan is the only global solution on the table and to us clearly offers the most benefit to the greatest number of TWA stakeholders.

IV. TWA's Final Chapter Ends on a Positive Note

As I look to the future of aviation, there are many chapters yet to be written. I believe, however, that the nature of TWA's final chapter will be viewed in years to come as having provided major benefits to the aviation industry. Among the ranks of our current employees, there are many young and talented people who have benefited from their apprenticeships under seasoned TWA veterans. They can take with them to American, and to every corner of the aviation world, knowledge and experience that is invaluable. When I consider this possibility becoming a reality for so many of our workers through this transaction, I know that all of our efforts will have been worthwhile. Indeed, TWA's legacy, if not its grand name, will be carried forward by its people.

Just as important, consumers will continue to see the same levels of service without the dislocation that would have otherwise occurred if a bankruptcy with a parceling out of assets had occurred. Indeed, this is the only way that public interest will be served in the long run.

Mr. Chairman, let me conclude by again thanking you for the opportunity to testify today. As I have said, we strongly believe this transaction should go forward. It is in the best interest of TWA employees, retirees, creditors, consumers, and communities served by both carriers. I would be pleased to respond to any questions.

The CHAIRMAN. Thank you very much.

Mr. Johnson, Chairman Johnson, welcome back before the Committee.

STATEMENT OF ROBERT L. JOHNSON, CHAIRMAN AND CEO, DC AIR

Mr. JOHNSON. Thank you, Mr. Chairman, Senator Hollings and Members of the Committee. I am delighted to appear here before you again today to talk about DC Air.

From the day that we announced the creation of DC Air, my vision for this ground-breaking company has remained intact: to build on the well-established service from 44 communities throughout the mid-Atlantic region to Washington's National Airport that approximately 3 million passengers a year have come to rely on; to provide safe, reliable, high quality service at competitive prices to customers and communities in the regions we serve; to compete vigorously on price and service in the communities that we serve; to facilitate the growth and economic development that accompanies air service; and to develop and maintain an airline that the Washington region will be proud to call its home town carrier.

In addition, as Chairman, CEO, and majority owner of DC Air, I pledged from my very first day to spend millions of dollars to create, own, and operate this new airline, America's first minority-owned air carrier in over 30 years.

Mr. Chairman, Members of the Committee, I am proud and happy to report today that we have made a number of significant strides forward in realizing the full scope of this vision. As you are well aware, from the first discussions of DC Air critics speculated that its proposed agreement with United for transition period resources, however brief and arm's length these may have been, might have compromised our goal of establishing DC Air as a viable independent carrier. This has all changed with our announced partnership with American Airlines.

American's recently announced agreement to invest in DC Air and to provide these transition resources proves that these theories could not be further from the truth. Make no mistake about it, the resources that American Airlines is bringing to DC Air—expertise, capital, and infrastructure—as it grows its operations here and throughout the eastern United States will go a long way toward making DC Air a powerful competitive and independent airline on day one of our operation.

By far the most important outcome of the DC Air-American Airlines partnership is the benefits it will afford our *customers*. Of prime importance will be the consumer benefits associated with the 20-year marketing alliance between our two companies. This will allow passengers traveling on DC Air to earn American AAdvantage frequent flyer miles which they can redeem on DC Air or anywhere in American's national network or its global route system. Thus, passengers flying on DC Air will reap the benefits of what many consider to be the premium frequent flyer program in the industry. In addition, DC Air passengers may enroll in American's airport lounge program, accessing facilities at National Airport, and indeed worldwide.

By adding its relationship with DC Air to its internal growth and announced acquisitions, American will become a major competitor for north-south traffic flows along the eastern United States.

Now, some of you may ask, why did DC Air choose to partner with American. We had received expressions of interest from a number of carriers regarding a partnership and entered into very detailed negotiations with several. While we could have chosen any of several different paths, I had the opportunity at a critical point to meet and get to know Don Carty, the Chairman of AMR, American's parent company. It became clear to me in that meeting and throughout our subsequent discussions that not only were the economic terms of the arrangement favorable to DC Air and the benefits to our passengers outstanding, but—and this was most important to me—but also that Don Carty and the American team truly understand what DC Air and minority ownership is all about and they are looking forward to being true partners with DC Air.

First and foremost, under the alliance with American I am the CEO of DC Air, and under my leadership DC Air will be an independent company. Let me be clear. DC Air has no obligation whatsoever to sell additional shares to American Airlines. American has purchased a minority equity stake of DC Air, ensuring that the airline will follow the vision I have set out for DC Air.

Under this alliance, American has stepped in to provide between 11 and 14 jet aircraft that will clearly help DC Air provide quality service to more destinations each day and has agreed to provide ground handling and other services to DC Air.

I have received some queries about the cost structure of DC Air under the arrangement with American. American will benefit from the success of DC Air through its equity investment and providing services at very competitive rates to DC Air. In addition, American has significant economies of scale in various areas that can be passed along beneficially to DC Air. Therefore, our costs will be fully competitive and our vision of competing aggressively in both service and fares is not only intact, but also greatly enhanced.

With the new support provided by American Airlines, DC Air will have all the resources necessary to be fully operational on day one, pending the closing of the merger.

Finally, as the majority owner of DC Air I believe it is critical to sustain and enhance the existing US Airways network, which has provided affordable, safe, reliable service to cities in the Northeast for so many years. Nothing in the American agreement changes my long-term commitment to these small and mid-sized communities.

Mr. Chairman and Members of the Committee, thank you for the opportunity to testify before you today.

[The prepared statement of Mr. Johnson follows:]

PREPARED STATEMENT OF ROBERT L. JOHNSON, CHAIRMAN AND CEO, DC AIR

Mr. Chairman, Senator Hollings and Members of the Committee, from the day that we announced the creation of DC Air, my vision for this groundbreaking company has remained intact:

- To build on the well established service from 44 communities throughout the mid-Atlantic region to Washington's National Airport that approximately 3 million passengers a year have come to rely on;
- To provide safe reliable, high quality service, at competitive prices to customers and communities in the region we will serve;
- To compete *vigorously* on price and service in the communities we serve;
- To facilitate the growth and economic development that accompanies air service; and
- To develop and maintain an airline that the Washington community will be proud to call its hometown carrier.

In addition, as Chairman, Chief Executive Officer and majority owner of DC Air, I pledged from our very first day to create, own, and operate this new airline—America's first minority-owned air carrier in over 30 years—because in my heart I believed it would be good for consumers, ensure competitiveness in air travel, and do right by the 44 communities we will serve.

Mr. Chairman, I am proud and happy to report today that we have made a number of significant strides forward in realizing the full scope of this vision.

As you are well aware, from the first discussions of DC Air, critics speculated that its proposed agreements with United Airlines for transition period resources, however brief and arms-length these may have been, might have compromised our goal of establishing DC Air as a viable, independent airline. This has all changed with our announced partnership with American Airlines. American's recently announced agreement to invest in DC Air and to provide these transition resources proves that these theories could not be further from the truth.

Make no mistake about it, the resources that American Airlines is bringing to Washington D.C.—an experienced staff, capital, and infrastructure—as it grows its operations here and throughout the Eastern United States will go a long way toward making DC Air a powerful, competitive, and independent airline on day one of our operations.

By far the most important outcome of the DC Air-American Airlines partnership is the benefits it will afford our *customers.* Of prime importance will be the consumer benefits associated with the 20-year marketing alliance between our two companies. This will allow passengers traveling on DC Air to earn American AAdvantage frequent flyer miles which they can redeem on DC Air, or anywhere in American's national network or its global system. Thus, passengers flying on DC Air will reap the benefits of what many consider to be the premium frequent flyer program in the industry. In addition, DC Air passengers may enroll in American's airport lounge program, accessing facilities in National Airport and worldwide.

Through the alliance with American, DC Air's customers will also have access to a vast network of new destinations. For example, our passengers will be able to fly from Richmond to National on DC Air, and then from National to New York or Boston on American Airlines' Shuttle service. Additionally, DC Air passengers will have direct access to the rest of American's network, which includes service to Chicago, Dallas and Miami. And, should American's proposed acquisition of TWA be consummated, passengers could also take advantage of convenient connections over Reagan National to St. Louis and Los Angeles.

The alliance with American will expand DC Air's reach from point-to-point service to and from Washington and connections up and down the East Coast, into an established network that spans the globe. In turn, American Airlines will get a strategic partner with a significant network in the east, operating out of Reagan National Airport, to complement its planned growth within the east. By adding its relationship with DC Air to its internal growth and announced acquisitions, American will become a major competitor for North-South traffic flows along the Eastern U.S.

While the benefits to passengers bode well for the success of DC Air, many of the operational aspects of the DC Air-American alliance will go a long way toward addressing of the broader public policy concerns raised about DC Air's viability as a stand-alone entity and our ability to enhance the competitive landscape on the East Coast.

As you may recall, our original plan for DC Air had been to manage a rapid transition into a network of 44 cities using 37 aircraft on our first day of operations.

We had arms-length arrangements with United Airlines to provide 10 wet-leased jet aircraft, as well as services including ground handling and other items, to ensure that DC Air had full access to all needed services on "day one" of operations.

Still, some observers of the process appeared concerned that any form of ongoing relationship with United Airlines, no matter what it was, somehow called into question DC Air's independence—in part, because United would be one of our major competitors in this region.

In response to those concerns, we at DC Air accelerated the process of entering into relationships with carriers other than United to provide these services. We had received expressions of interest from a number of carriers regarding a partnership and entered into very detailed negotiations with several. While we could have chosen any of several different paths, I had the opportunity at a critical point to meet and get to know Don Carty, the Chairman of AMR, American's parent company. It became clear to me in that meeting, and through our subsequent discussions, that not only were the economic terms of the arrangement favorable to DC Air, and the benefits to our passengers outstanding, but also that Don Carty and the American team truly understand what DC Air is all about and that they are looking forward to being our partner.

First and foremost, under the alliance with American, I am the Chairman of DC Air and under my leadership DC Air will be an independent company. American has purchased a minority equity stake, 49 percent, of DC Air, ensuring that the airline will follow the vision we previously have so clearly set out for DC Air.

Under this alliance, American Airlines has stepped in to provide between 11 and 14 jet aircraft that will clearly help DC Air provide quality service to more destinations each day and has agreed to provide ground handling and other services to DC Air during its transition period.

Although I believe most of you view our independence from United in a positive light, I want to underscore to you that our alliance with American will only ensure that we will be able to compete aggressively in both service and fares with other airlines. United will no longer help to provide transition services. United is our rival, our foe, our adversary. And, we will face our competitors, including United, with the support of American Airlines behind us as we go into battle.

I have received some queries about the cost structure of DC Air under the arrangement with American. American will benefit from the success of DC Air through its equity investment, and is providing services at very competitive rates to DC Air. In addition, American has significant economies of scale in various areas that can be passed along beneficially to DC Air. Therefore, our costs will be fully competitive and our vision of competing aggressively in both service and fares is not only intact, but enhanced.

The American Airlines-DC Air alliance will ensure vibrant competition throughout the Washington area. Without this alliance, the metropolitan area would have one primary traditional carrier—United Airlines—offering nonstop service to a variety of destinations and connections to worldwide destinations from its hub at Dulles International Airport. Of course, other airlines, notably Air Tran, Delta Air Lines and Southwest Airlines, would continue to serve the metropolitan area, but each of these airlines offers a more limited scope of nonstop destinations to Washington passengers. Instead, this alliance will bring into this region a significant new competitor, DC Air, with the support of a traditional carrier, American, which in combination will become the largest presence at Ronald Reagan Washington National Airport. This will provide for intense competition for both East Coast and worldwide passengers that will keep prices down and help ensure high quality service for area travelers.

And, with the new resources provided by American Airlines, DC Air will have all the resources necessary to be fully operational on "day one," pending the closing of the merger. When it is operational, DC Air will provide competitive air service to 44 communities—cities that, for the most part, currently enjoy direct access to the Washington area. As the majority owner of DC Air, I believe it is critical to sustain and enhance the existing US Airways network, which has provided affordable, safe, reliable service to cities in the Northeast for so many years. Nothing in the American agreement changes my long-term commitment to these communities.

When I agreed to build and run DC Air, I strongly believed it would prove to be a strong, independent airline. The new alliance between DC Air and American Airlines brings us closer to achieving the goals I set out when I agreed to build and run DC Air—to provide high quality, safe, reliable air travel, to help preserve competition in the airline industry, and to make air travel affordable.

Thank you for the opportunity to testify before you today.

The CHAIRMAN. Thank you very much, Mr. Johnson. Thank you for coming back before the Committee again.

Mr. Leonard, welcome.

STATEMENT OF JOE LEONARD, CHAIRMAN AND CEO, AIRTRAN AIRWAYS

Mr. LEONARD. Thank you, Mr. Chairman and Senator Hollings and Members of the Committee. Thanks for the opportunity to be here again. You know, the last time I was here was about 6 months ago and we were talking about the United-US Air merger. I did not believe at that time that it would be approved in the form that it was presented. But I can tell you, I never in my wildest imagination dreamed that the solution to that problem would be American Airlines and United Airlines replacing the Civil Aeronautics Board.

At that time I was concerned about industry consolidation, higher fares, poorer service, failure of more low-cost carriers. Unfortunately, all of those predictions have come true since I was here last.

We were talking last night, you know, if the situation continues unchecked I will soon be running the fifth or sixth largest airline in the country, but I will only have 1 percent of the market share.

I would like to make a prediction about what will happen if nothing is done. If the government sits by and takes no decisive action soon, then the ultimate consolidation will take place before the end of this year, and consumers had better fasten their seatbelts and hang onto their wallets.

The United-American-US Air agreements cannot be separated from American-TWA. American is the bridge that links all of these deals together.

Let us also understand that this will be the biggest consolidation in the history of American aviation. It involves the two largest carriers in the world carving up the U.S. market. Delta will have no choice whatsoever but to acquire pieces of Continental or Northwest, thus leaving 80 percent of the passenger seats in this country in the hands of three companies.

Look at a couple of the elements of the agreement between American and United. They are fixing fares and schedules in the shuttle market. They agree to limit each other's growth. They agreed to code-share in competitive markets. Do you think that is going to be real competition? I do not think so. From the consumers' perspective, they will pay much higher fares and have poorer service and no choice or little choice.

AirTran is a survivor that demonstrates what a strong new entrant can do for the consumer when we have access to markets. Each year AirTran saves consumers in the Atlanta marketplace $700 million in air fares because we have critical mass in Atlanta.

I hear a lot about the Southwest effect: You do not really need to worry about competition because Southwest is around. And Southwest does discipline fares in about 6 percent of the markets, but let us look at a couple of examples of the Southwest effect. From Baltimore to Hartford the fare is $120 round trip. How about from DCA to Hartford? The fare there is $628. Where is the Southwest effect in DCA to Hartford? It does not exist.

Let us take a look at a couple of fares where American and United go head to head, really battling out, really competing strong. Chicago to Washington National, the fare is $1439. What about Chicago to DFW, two hubs, head to head competition, lots of frequency? Guess what, the fare is $1439 last week, exactly the same as the Washington market. If the government permits the American-United combination in this form, the public can expect the kinds of fares that they see in those two markets all over the country.

Size matters, as Mr. Carty said, in this business, and that UAL and American are willing to pay so much for these vital assets, by doing so they block competitors' ability to develop a network on the East Coast, which is the end product of the United-American agreements as they are currently structured

AirTran and other low-fare carriers need access to gates and slots in order to discipline the fares and to benefit the consumers and the communities up and down the East Coast. We need enough to generate a network. There are certainly enough to go around. American and United will control over 1,000 slots at Washington National and LaGuardia if this deal goes through, or in other words 65 percent of all the slots at those two airports.

With a meaningful number of slots and gates at Washington National and other key airports, low-fare airlines like ourselves could bring $600 million of benefit to the consumers and the East Coast and in particular in the smaller cities.

Deregulation was supposed to provide a level playing field for healthy competition. At stake right now is the wellbeing to the American public for the generation to come. At stake is hundreds of millions of dollars in savings that can be put in the pockets of consumers. At stake is whether small- and medium-sized cities can revive their economies with the new business opportunities that come with low-fare competition and service.

Mr. Chairman, I urge you to give the consumer some hope for a better day by using your authority to urge the Department of Justice and the Department of Transportation to make open access the hallmark of decision making in these matters. We cannot win the battle of competition if we are not permitted on the battlefield.

I also would like to add that we are not opposed to mergers and acquisitions. We think they are going to happen either through an orderly process or through bankruptcy. But consolidation must come with the award of a large block of gates and slots and other public assets to low-cost competitors so that we can keep the marketplace honest.

Mr. Chairman, thank you very much for the opportunity to be here this morning.

[The prepared statement of Mr. Leonard follows:]

PREPARED STATEMENT OF JOE LEONARD, CHAIRMAN AND CEO, AIRTRAN AIRWAYS

Mr. Chairman and Member of the Committee, I thank you for your invitation to appear today. I will come straight to the point.

Since I last had the privilege of testifying before the Committee some six months ago, I believe most of the things I warned about have taken place, or are taking place: increased momentum for industry consolidation, higher fares, poorer service, and the failure of more low-fare carriers.

Permit me to make a new prediction: unless the Congress and/or the Executive Branch takes decisive action soon, then by the end of the year this party will be over. The consolidation agreements will be virtually complete in a legal sense, labor agreements for merging carriers will be under negotiation, and consumers had better fasten their seat belts—they will be in for a very rough ride and a very hard landing.

That would be a tragic failure of public policy, and it will be as significant to the consumer as was the deregulation of the airline industry more than 20 years ago—but with a much different and unfavorable impact.

Let me remind the Committee that with one important qualification, I do not oppose airline mergers and consolidations. I recognize that the jobs and the service provided by the men and women who work in the airline industry in St. Louis or Pittsburgh or Washington are just as important as AirTran jobs in Atlanta or Orlando.

I also recognize that without consolidation, there will be bankruptcies, service disruptions, job losses, and, in the end, the major carriers will have picked the bones of the failed carriers. We would end up with the same anti-consumer landscape we can expect if all the mergers and acquisitions on the books today are carried forward, except worse. However, this consolidation cannot proceed without accommodation for low-cost competition.

Let me take a moment to talk about the specific proposals before the Committee this morning.

From a public policy perspective, the United/American/US Airways agreements cannot be separated from the American/TWA acquisition.

American is the bridge that links all of the proposals.

Let us also understand that this is the biggest consolidation in the history of american aviation. It involves two of the largest airlines in the world carving up the U.S. market. If these series of transactions go forward there will be no basis for stopping Delta from acquiring Northwest and/or Continental and leaving 75 percent of the passenger seats in the nation in the hands of three airlines.

That level of concentration leaves no room to even pretend that there will be price competition. History tells us that the major carriers support price maintenance not price competition.

Look for just a moment at the elements of some of these agreements.

The fixing of fares and schedules in the shuttle market—clearly identified as one the terms of the American/United agreement—is unprecedented as is the level of cooperation that the government is being asked to endorse. It takes the concept of "trust me" to new heights.

All of this is taking place when competition is at the lowest point in twenty years.

From the consumers' perspective it will not matter how American got to control the slots at Reagan Washington National Airport or how United and American got to set fares and schedules on the shuttle. The only thing that will matter is why they are paying so much for airplane tickets with so little choice of airlines.

American and United are trying to grow through the acquisition of weaker competitors.

Mass matters. The single carrier service American and United tell us provide benefits to the consumer also means that each carrier controls 25 percent or more of all seats sold in the nation.

Mass means they control gates and through slots the airways.

Unless the government acts aggressively now to protect the consumer and to provide to low cost carriers like AirTran access to scarce basic facilities—gates and slots—competition will suffer and prices will rise.

The airline marketplace belongs to those airlines that have critical mass.

That is marketplace reality.

The government must not allow the major airlines to effectively block the ability of low fare carriers like AirTran to gain critical mass .

Mass means networks—the ability to flow passengers over a hub to multiple destinations—whether that hub is a traditional one or an effective one as is the case with the somewhat linear Southwest structure.

Southwest and new entrants are the only carriers that offer effective fare competition, yet the number of new entrants is at an all time low just as the major carriers are consolidating even more to protect their franchise.

AirTran is a survivor that demonstrates what a strong new entrant can do for the consumer when it has access to markets.

AirTran each year saves the Atlanta consumers more than $700 million dollars in airfares because we have critical mass in Atlanta—mass that we got only because Eastern Airlines went bankrupt and freed up 22 gates. That does not happen very often and the American consumer should not have to depend on happenstance to have access to low fare airlines.

Southwest disciplines fares in some markets because it has a network that immediately allows it to enter a market and provide consumers with destinations all across its system. Its network gives Southwest its strength—it can compete across a broad spectrum of routes.

JetBlue is providing relief to small communities because the DOT awarded them 75 slots at JFK. That type of access is critical. Does anyone believe that American or United will bring this same kind of cost savings if they are allowed to control these hundreds of additional slots?

Blocking competitors ability to develop a network is the end product of the United/American agreements as they are presently structured.

Throughout the northeast, american and united would effectively control access to gates and slots. At no place is that more evident than at Reagan Washington National Airport.

Consumers traveling out of national pay premium prices because access to gates and slots is tightly controlled.

Southwest may sell "walk-up" roundtrip tickets out of Baltimore to a city like Hartford for $120, but Southwest's fares have in no way stopped US Airways from charging $628.50 for that same ticket. That $500 dollar plus premium reflects the importance of National as a unique facility precisely because access is controlled by reason of government licensing of access—slots.

If the government—whether it be the Department of Justice in its antitrust review or the Department of Transportation deciding to sit on its rights and do nothing—permits the American/United combination in the form proposed, those kind of premium fares will be the name of the game in the northeast.

Those premium fares explain why both airlines are prepared to pay so much for these assets and put up with all of the labor and operational problems that will follow—in the current form of the mergers—the major airlines win and the consumer loses big time.

That is marketplace reality.

That is the effect of government decision making in these cases.

AirTran and other low fare carriers need access to gates and slots to discipline fares for the benefit of consumers and communites up and down the east coast.

The AirTran business model works as well in Washington as it does in Atlanta.

With a meaningful number of slots at Washington National, AirTran would bring no less than $600 million dollars in savings to consumers traveling through and to Washington National Airport whether they originate in Charleston West Virginia or Rochester New York. Significant access to LaGuardia slots or gates in Philadelphia allows us to provide savings up and down the east coast but without access we can only stand outside and watch the major airlines extract premium prices from captive consumers.

We believe that the choice for the government is simple, let American and United create fortress northeast or let consolidation go forward with meaningful protections for the consumer.

That is marketplace reality.

Deregulation was supposed to provide a level playing field and healthy competition. The deregulation act charges the Department of Transportation with responsibility for facilitating new entry and competition in the airline industry. While this is the mandate, in reality DOT has done virtually nothing to help domestic competition and new entry except acting under the mandate of the Congress.

At stake right now is the well-being of the American flying public for a generation to come.

At stake is hundreds of millions of dollars in savings that can be put in the pockets of the consumer.

At stake is whether small and medium sized cities can revive their economies with the new business opportunities that come with competitive, low fare service.

I urge you to give the consumer some hope for a better day by using your authority to urge the Department of Justice and the Department of Transportation to make open access the hallmark of decision making in these matters. We cannot win the battle for competition if we cannot get on the battlefield.

Thank you.

The CHAIRMAN. Thank you very much, Mr. Leonard.

Mr. Levine.

STATEMENT OF MICHAEL E. LEVINE, ADJUNCT PROFESSOR OF LAW, HARVARD LAW SCHOOL

Mr. LEVINE. Mr. Chairman, thank you very much.

The CHAIRMAN. Would you take the microphone, please.

Mr. LEVINE. Sorry.

The CHAIRMAN. Thank you.

Mr. LEVINE. Mr. Chairman, Members of the Committee: Thank you very, very much for inviting me. I think this is a very important subject and I appreciate the chance to speak to the Committee about it.

I am here as a Committee witness. I have not been paid for or coordinated my testimony with anyone. I am here because I have a lifetime commitment to airline deregulation.

I have a longer statement for the record, which I will not read. It includes information on my background that you may find interesting.

The CHAIRMAN. Does that include the work with the CAB on airline deregulation?

Mr. LEVINE. It does indeed. I was one of the early academic writers urging airline deregulation. I was effectively the chief of staff at the Civil Aeronautics Board during Fred Kahn's and Marvin Cohn's transition through deregulation, and I have been in a sense a practitioner because I have been at three different airlines: one of the transitional network carriers; a new entrant, New York Air; and later at the fourth largest network carrier.

I am here because I think that the American-United-US Air deal essentially threatens airline deregulation and the results of deregulation. I ought to make clear: I have no particular problem with the American-TWA deal. I do not think it eliminates competition in a meaningful way because I think TWA is, in fact, a failing company. I do not think it is a particularly good deal for American and its shareholders for reasons that are in my testimony and that I will be happy to answer questions about.

But my concerns about whether it is a bad deal, which otherwise I would leave to the marketplace, largely lie in the evidence this deal may provide for understanding American's motivation for working with United in the US Airways deal. I think the TWA deal, as I say, does not make a lot of sense on its own. American wants TWA's assets partly because, as Mr. Carty has already told you this morning, network size and scope matter and American would like to grow a little bit, to move up on United.

The East Coast assets and slots and gates of TWA are particularly important to American, for reasons I will come back to. But I think that in addition and perhaps even more so, American conceives the TWA deal as something that can be used to cast a sort of "failing company" halo over the larger US Airways deal. I do not think that the larger deal should be seen that way at all.

I have a different interpretation of what is going on. I think this is meant to be the end of the airline ubiquity arms race that started after deregulation and that basically was continued by American and United as the survivors of the pre-deregulation Big Four. These also included Eastern, now gone to its reward, and TWA, about to go to its reward. American and United engaged in a race for unilateral rivalry in the 1980's that almost bankrupted the industry, because the industry agreed with Mr. Carty that network size mattered and did not feel it could be left far behind. Everyone engaged in a race for ubiquity. That was ended when the recession of 1990 through 1992 brought near financial ruin on the industry as a result of this expansion race.

United through its offer for US Airways made a unilateral move to try to win the ubiquity sweepstakes in a way that would end the game. That effort has run into difficulties due to competition concerns which are entirely justified. American has now countered, in effect, by offering an armistice. They want both airlines to use the East Coast assets of US Airways, which they will divide between them, and the split monopoly over Washington to build a fortress wall around the East Coast, which is a very important national source of traffic and a very important element of any network. Traffic from the big Northeast cities creates volume, which can be used to increase the size and frequency of a hub system, so as to gain an advantage on your competitors. An airline with a larger network can get more corporate contracts. It can have more effective travel agency commission override system and its frequent flyer program becomes more important than those who have finished in the dust.

More importantly, this deal is designed to accomplish this permanently, because once the East Coast has been divided between American and United in the way that this deal proposes to divide it, I believe that Delta and Northwest and Continental will not be able to construct a network that will be comparable in power. The existing situation, in which the big airlines in effect operate as kind of super-regionals, in which they have large areas of regional strength and then reach to the East Coast and compete vigorously, will have gone away.

You can ask, "what evidence do we have that this interpretation is correct?" I think there are three important pieces of proof that are in the deal: One is the prices which are being paid by both American and United, plus the transition costs, the service disruption, the systems integration costs that are going to be involved in these deals. It is clear to me that these airline expect to get revenue premiums, which means they hope for monopoly profits that come from customers, to finance these payments that they are making.

Two, it is interesting to me that United would rather let its so-called arch-rival, American, provide competition at Washington, D.C., than it would Continental, which has offered to do so (which would allow it to gain on this Big Two that is being created) or AirTran, which as Joe Leonard has suggested would provide price competition, or any of the several other airlines that I have reason to believe have expressed interest behind the scene and which Mr. Johnson referred to in his discussions.

Three, United has offered to share the shuttle with American. That is one of the keys to getting control of the Northeast because the folks who fly the shuttle are business people what buy tickets to other places and it is very important to have them in your frequent flyer program. It is interesting to me that United would be willing to share one of the crown jewels of the US Airways acquisition. This suggests that they expect something less than an all out competitive war.

I think it is important to note that they have offered to share the crown jewel conditionally, only if American does not get bigger than United as a result of some subsequent acquisition that it might make. If that happens, then, interestingly enough, the shuttle and other acquired assets go back to United to have for its own. To me, this whole thing just clearly represents a kind of, as I say, an end to the ubiquity war.

As my friend Joe Leonard suggested, I do not think you can count on Southwest Airlines to provide discipline to this Big Two that is going to be constructed. Southwest is a great airline, there is no question about it. It provides a service that is very important to a lot of people. But first it is not a perfect substitute for a network airline. There are a lot of places it does not fly to. It expects its customers to drive to it to get its low fares. For many business men and women that is not a very convenient way to do business.

Southwest does not provide very convenient connections. It does not provide some of the services that network airlines provide. There is room in the system, important room in the system, for Southwest Airlines. But no one should regard it as a perfect substitute for network air service.

Second, it should be pointed out that, although Herb Kelleher is a man of legendary benevolence, I think he is still running his airline to make a profit, and if a price umbrella is provided him by a duopoly in the airline business his prices are likely to go up because he can still maintain his competitive advantage if he does so and he will make more money.

Ultimately, I do not think you can count on Southwest as the answer to the antitrust problems that this deal presents.

So I think consummation of this deal should be prevented under the antitrust laws. If Justice is unwilling or feels itself unable to do it, I think Congress should do it. I think this is a very serious threat to deregulation. I invite this Committee to take a further interest in it. I congratulate you for holding this hearing.

I thank you for inviting me and I will be happy to answer any questions you might have.

[The prepared statement of Mr. Levine follows:]

PREPARED STATEMENT OF MICHAEL E. LEVINE, ADJUNCT PROFESSOR OF LAW, HARVARD LAW SCHOOL

Mr. Chairman and Members of the Senate Commerce Committee: Thank you for giving me the opportunity to testify before you today at what I believe is a critical point in the development of the deregulated airline industry. I testify at the invitation of the Committee as a private citizen and not on behalf of any airline, industry group or other organized interest. My reason for testifying is simple: I have dedicated most of my career first to bringing about a competitive deregulated airline industry and then to demonstrating through my own personal efforts that it is possible for a well-managed airline to survive and prosper in a competitive environment. I see a threat to the continued success of airline deregulation, and I hope to play some part in countering that threat.

I am at present a member of the faculty of the Harvard Law School, teaching courses in regulation and international joint ventures. I have attached a detailed biography to this testimony for your information, but let me say briefly that I have had the unusual opportunity to study, to regulate and to work in the airline industry. This experience has included work as a dean and scholar who has advocated and continues to advocate deregulation at USC, Caltech, Yale and Harvard. It also included a position as the senior staff member at the Civil Aeronautics Board under Alfred Kahn and then Marvin Cohen during the most pivotal deregulation period. And I also have had the opportunity to participate in the industry as a CEO or senior executive of a transitional network airline (Continental), a new entrant airline (New York Air) and finally at the fourth largest airline in the United States (Northwest).

I am very concerned about the consequences for industry competition and ultimately for consumers of the proposed division of USAirways between United Air Lines and American Airlines.

Before I discuss that transaction I should make clear that the "companion" merger between American and TWA on its own presents no serious competition problems. That TWA is a failing company seems beyond doubt. The TWA deal may present difficulties for American in terms of labor, fleet and systems integration. Those problems may present service problems for the traveling public but if they materialize, the public can deal with them by avoiding American. They will still have that choice because the American-TWA transaction will not change the structure of the industry and does not present a threat to the competition that is necessary for deregulation to succeed as a public policy. This matter should be left to the marketplace and the bankruptcy courts.

American has justified its merger with TWA on its own merits at the same time that it has presented it as part of a strategic package that includes American's agreement with United to divide USAirways. It seems clear to me that the most important purpose of the TWA deal is to help give a "failing-company" cast to the whole four-airline transaction, and to provide political cover (preserving 20,000 jobs and a large-airline hub presence at St. Louis) to politicians and government officials as they consider a total transaction much more difficult to justify on competition grounds. The second major benefit to American is not the chance to operate a St. Louis hub, but rather to use TWA's slots and facilities at congested East Coast airports to bolster American's New York and East Coast strategic position and to use TWA aircraft to achieve market share parity with United as part of the Big Two strategy discussed below.

The significance of the TWA transaction is that a closer look at it raises suspicions about American's strategic motives. On its own, the TWA transaction is difficult to justify commercially. TWA has been carefully examined as an acquisition candidate by every major airline (more than once, in many cases), and I believe that those studies all came to the same conclusion: while St. Louis is well-located and can support a hub of some size, it would be very difficult for a "normal" network airline to make any significant profit there.

First and most important, operating a hub on top of Southwest Airlines means that normal hub economics are impaired by the inability to charge normal hub fares to short-to-medium haul business travelers, and as Southwest's system continues to evolve out of its previous short-haul, point-to-point mode, that effect becomes more and more severe. Just ask America West, which has had considerable difficulty maintaining at Phoenix a revenue base adequate to support a significantly profitable hub operation, even at its very low costs. When you add into this equation American's labor costs and the transition costs of labor, systems and fleet integration, it's difficult to believe that American's better credit and better fuel purchase position and the overhead savings from eliminating TWA's management infrastructure make this transaction taken by itself additive to American's earnings or worth the risk. I know these numbers didn't work for anyone else, and would be surprised to learn that they suddenly make sense on their own for American.

Second, this is clearly a case where American is acting in concert with United to achieve jointly-shared strategic goals. If United was only interested in solving the Washington, DC part of the antitrust problem presented by its own USAirways deal, any number of other airlines would have been willing to help them out. But rather than Continental or AirTran, who have publicly indicated a willingness to work with Robert Johnson to produce a DC Air that would be a full-blooded competitor to United (or rather than the couple of other airlines who are rumored to have expressed serious interest), United has chosen to work with the airline that is its supposed arch-rival and that should be its most difficult competitor from the standpoint of network coverage ("scope"). In fact, when the transaction is taken as a whole United has cooperated in fashioning a deal that represents a giant step forward for American in achieving its stated goal of network ubiquity even as it impairs United's attempt to build a uniquely ubiquitous position. Why would United do this? To understand, I think we need to look at a bit of history.

American and United are what remain of the prederegulation "Big Four". Eastern has gone to its reward and TWA, shrunk to a shadow of its former self, is about to follow. Both were victims not only of their own managements' strategic mistakes, but also of their inability to persuade their own labor forces to adapt proactively to the changed circumstances of deregulation. United and American, facing the same concerns about their ability to survive deregulation given their high costs, adopted a different management strategy: they persuaded their labor forces in the postderegulation period to reach accommodations that lowered marginal labor costs ("B"-scales, ESOP, periodic scope relief, etc.) and allowed fleet and system flexibility in return for assurances of growth, producing more job security and richer lifetime career paths for employees. They coupled this with adoption of a "ubiquity" strategy, in which the size and reach of their networks would allow them to meet almost every air transportation need of every airline customer. This ubiquity would be used to differentiate themselves from new entrants for business travelers and to gain a revenue advantage over other network competitors. United announced shortly after deregulation that it had become the first airline to serve all 50 states. American moved to Dallas so that it could serve a very large, centrally located, facility-unconstrained O&D market as a national hub. The idea for both American and United was that they would ultimately overwhelm smaller network competitors as customers and travel agents chose to sign contracts with and use the frequent flyer benefits of the airline that could satisfy the largest portion of their needs.

On their way to unchallenged ubiquity, two things happened. Other network competitors saw what was happening and refused to roll over quietly. First Texas Air, then Delta, Northwest, Allegheny/USAir (remember the Piedmont merger and the name change?) and Continental on its own attempted expansions designed to enhance their own ubiquity and thus survivability. A sort of ubiquity arms race ensued, which caused severe self-damage to more than one participant and nearly destroyed the entire industry when the economic expansion of the 1980s segued into the recession of the early 1990s. In the process, Delta became large enough to approach American and United in size, but more important, the recession-induced stunting of the growth process evolved the industry into an "almost-national" mode, with each successful network airline building and defending regional core positions that supported a large but incomplete national hub system. The traveling public benefited hugely from this process (shareholders benefited less!). The almost-national systems were very large and provided many of the benefits of complete network scope. People in spoke cities often had a choice of as many as half a dozen competing hub carriers that could meet a particular trip need, hub-located travelers could get nonstop service to 80 or more destinations comprising most of their travel needs and most travelers could meet virtually all their needs by concentrating their business on two systems, for which they were rewarded with frequent flyer benefits they valued greatly.

But from United's and American's perspective, this was not such a splendid state of affairs. They had built their labor strategies around paying labor for growth and the ability to use their network strength to capture revenue premiums (monopolistic rents). Growth was slowing as it had become clear that capacity expansion would be defensively matched and there was not enough new business to support profitable expansion for American and United relative to the rest of the industry. The national market became more concentrated among the top five network airlines and Southwest, but almost all of the incremental share went to Southwest, Delta, Northwest and Continental. The development of alliances by smaller airlines as a way to achieve many of the benefits of network size without the risks of overcapacity further eroded their revenue premiums. The net result of twenty years of deregulation was NOT that American and United had become uniquely ubiquitous airlines, but rather that they had come to share the network industry with several competitors that not only wouldn't go away, but which constrained the possibility of further share expansion. For American and United, the strategic question became: how can we (either American or United or both) gain a network size advantage that can't be duplicated and eroded and which will yield monopoly rents to support our very high costs?

Both airlines came to the conclusion that the key was the East Coast: United already dominated network service on the West Coast, but the West Coast has relatively few cities and while those cities wouldn't support more than one network (as American repeatedly found out through expensive tests—the Air Cal and Reno acquisitions and the San Jose north-south hub), its relatively uncongested, separated airports were ideal for expansion by Southwest. Further competitive shifts toward American/United were unlikely there. Delta's Atlanta hub operation along with expansion by Southwest and AirTran made the Southeast unpromising. The midline of the country provided as many opportunities to Continental and Northwest as to American and United, especially given the constraints at Chicago-O'Hare.

By contrast, the East Coast has a variety of interesting features which might allow it to underpin a sustainable network size and scope advantage which could be leveraged into a dominant position: a large part of the nation's population and travel origin is located there. Airports are congested and facilities tight, making substantial matching expansion by network competitors difficult and substantial discount competition at the primary business airports nearly impossible. Four major population concentrations are the focus of much of the business traffic: Boston, New York City, Philadelphia and Washington. Northwest has no presence there except through the Continental alliance. Continental's and Delta's strength is largely limited to Newark (Continental) and north-south and transatlantic service (Delta). Transcontinental business is already dominated by American and United. Continental has only been able to build a significant transcontinental business from its Newark hub using narrowbody aircraft and Delta has been unable to make a significant dent in these markets. United has built a hub at Dulles and American has made a significant effort to build its presence at Boston, but neither of these efforts have produced a sufficient increment in East Coast presence to allow unduplicable network expansion that could cast a halo over the entire United States system.

American started to build an alliance with USAirways, the only airline with strategically-located sufficient mass that could make a difference to its network strength. The alliance involved codesharing, a frequent flyer deal and computer systems integration which lowered American's costs. Northwest and Continental built an alliance which made Northwest a much stronger competitor to United in the Midwest and over the Pacific and strengthened Continental's position in New York. These developments concerned United greatly. United was offered the opportunity to do something decisive in response by USAirways management's conclusion that its structural and cost problems couldn't be overcome without major flexibility by its unions, and its consequent decision to save its shareholders by bailing out after an attempt to reach union accommodation failed. The result was the United/USAirways deal.

What United expected to get out of the deal was an effective monopoly in Washington and Philadelphia, a greatly enhanced position in Boston and New York, and a major frequent flyer presence in the very important Shuttle markets. It hoped simultaneously to strengthen its revenue position vis-à-vis American, achieving through system market power what it had never been able to achieve through service and operations and to finally separate itself from the increasing competition offered by Delta, Continental and Northwest. That United paid too much is a tribute to Stephen Wolf's bargaining skills. That it did the deal without getting the union consents that would have helped manage transition costs is a confirmation of the priority that United's management gave the deal and how much impact on competition they expected it to have. There are many who think that this transaction might have in the end cost so much that it wouldn't have made a profit for United. That the costs of integrating the two airlines might have been such that its shareholders might not ultimately have benefited does not mean that there were no monopoly profits to be made, but only that the monopoly profits would be distributed among USAirways shareholders, United's labor force and Robert Johnson.

The only problem with all this is that the United/USAirways deal, despite its beautifully prepared political campaign, appeared to be in danger of failing. The DC Air "cure" to the Washington problem was not passing the laugh test. No one seriously believed that a United-supported DC Air with a large commuter component was likely to provide significant stand-alone competition to United in Washington. Offers of "help" by Continental and Airtran put United between the devil and the deep blue sea with respect to its transaction goals. Giving Continental a strong Washington position was the opposite from what United was trying to achieve in redistributing network system strength away from its pesky pursuers. And allowing a discount airline like Airtran to operate from the business revenue heart of its East Coast hub strength (bad enough to have Southwest at BWI!) would be very damaging to United's Washington economics and would make the transaction even more expensive by a substantial margin (in much the way that Southwest's presence at St. Louis makes the TWA transaction expensive for American).

American, with the prospect of losing its USAirways relationship and of seeing its United rival get a structural lock on a superior network position, offered United a brilliantly-conceived truce that was much more valuable to United than a failed deal and a continued war with Delta, Continental and Northwest. In effect, it offered to jointly share ubiquity, establishing a Big Two protected from imitation by East Coast facilities constraints and antitrust barriers to further merger. With the TWA deal and the deal as American and United have structured it, American and United would be almost exactly the same size at about 25 percent of the national market. Each of the Big Two could sustain a revenue premium relative to Delta, Continental and Northwest and generate network monopoly premiums to help stave off the economic impact of Southwest. Neither would have the incentive to erode those rents through price competition with the other (because little relative share gain would be possible), so pricing discipline would be maintained without collusion. While there would be a possibility that Delta or Continental might try to defend itself by combining with Northwest, none was a failing company and the Justice Department could be expected to be hostile, given its record in the Northwest/Continental control case. Paradoxically enough, the United/American joint monopoly position could be defended with the antitrust laws!

Even if their rivals could merge, no one would have the combination of Boston, Philadelphia and Washington strength available to the Big Two and could achieve the same system leverage. American could make itself stronger in New York through the TWA deal, achieve near-parity in Washington and Boston, and concede Philadelphia. It could make excellent network use of the Washington and other Northeast slots and gates it gets in this deal because of its success in using regional jets to maintain presence on mainline routes. Its ability to sustain a network advantage over "the others" would be assured. United would strengthen its position in Washington, Boston and New York, gain control of key facilities and slots, and build an East Coast North/South system. For both American and United, rivalry with each other along nonprice dimensions while each had market power relative to the rest was an attractive alternative to the status quo.

The Big Two position that these transactions would create is likely to last a very long time. The large pool of customers available in the Northeast and the ability to use the scarcity of slots and gates at its congested airports to lock them up will make it impossible to duplicate the Big Two position that American and United will share. No comparable opportunity will be available to other big network airlines and therefore no other network airline will be able to match United's and American's ability to offer corporate contracts, travel agency and internet incentives and frequent flyer benefits. Over time, Delta, Northwest and Continental will find it increasingly difficult to capture East Coast business passengers, providing less flow at their hubs and supporting less service than American and United will be able to sustain. The gap between American and United and the "others" will grow.

Among the strongest pieces of evidence that this narrative captures what the participants predict and intend in this deal is the treatment of the USAirways Shuttle, which is a crown jewel in any network scope strategy. The Shuttle is used primarily by a group of business travelers who are also the ones most likely to buy high-priced tickets to elsewhere from Boston, New York and Washington. In Delta's hands, the other shuttle is one of the assets most valuable in its efforts to move toward network parity with American and United. As a potential source of monopoly dominance, the USAirways shuttle is wasted in USAirways' hands because USAirways doesn't have the complementary system strength to take advantage of it. In fact, the Shuttle doesn't even serve Philadelphia, which is USAirways focus for much of its valuable business flying! American had a temporary advantage over United through its alliance with USAirways. United grabbed it back. United's giving up exclusive control of the network value of this Shuttle only makes sense in the context of a shared-dominance strategy in which both airlines see its principal value as enhancing their ability to suppress competition on the rest of their networks. This view of the transaction is confirmed by the fact that United gets to keep all of the Shuttle if American concludes an acquisition that makes it bigger than United!

This discussion doesn't deal with all of the potential objections to this transaction, some of which are common to the United/USAirways transaction as well. For example, public vulnerability to labor disruption is increased as more of the system falls into fewer hands. The public consequences of a job action on an airline so big that the rest of the system simply cannot absorb its business are very serious, as are the consequences of the associated imbalance in bargaining power. I have tried instead to focus on the subtle and complex competitive dynamics that underlie this transaction in an attempt to explain why this is not just another merger and just another rescue of some threatened airline jobs. (On that subject, I should say that the notion that USAirways is, like TWA, a failing company is entirely wrong. Faced with no alternative, management and labor could work together at USAirways to achieve costs and revenues that would enable it to survive, although some surgery might be necessary. But that's another story for another time.)

What can be said in favor of this transaction? Only that if consumers prefer to concentrate their business on one very large system, we should accommodate them. And there is no doubt that some consumers would prefer to do so, especially if all other things were equal. But all other things will not remain equal. This convenience will come at the price of choice and long-term competition. There are often conveniences to monopoly, as anyone who used to have only one number to call when they wanted to discuss their phone service will attest. But there are benefits from competition which have generally been judged superior as a matter of public policy. If one compares the utility to consumers of having competitive choices among airlines, almost any two of which can satisfy almost all their needs, with the "convenience" of one-stop shopping in a duopoly, I believe that most consumers would prefer competition. That comparison is reflected not only in our antitrust laws, but in the regulatory policies of the past twenty-five years.

It has been urged by at least one observer that we need not be concerned about loss of competitive pressure in the network business because Southwest in particular and other low-cost airlines in general represent a large enough share of the business to discipline United and American. I suppose that the first rebuttal is American and United clearly don't agree with him. It's difficult to justify the cost commitments and vulnerabilities which this transaction entails for American and United without assuming that they believe that they will earn substantial monopoly benefits from the transaction.

There are good reasons for thinking they may be right, even if in the end the transition and labor costs of the deal are so large that it ultimately doesn't benefit their shareholders:

First, although Southwest and its ilk offer a valuable service to their passengers, it is not a service equally valuable to all passengers. These airlines do not have significant presence (indeed, Southwest has *no* presence) at the very congested and constrained airports that are the principal focus of this transaction. Business travelers value and will pay for airport convenience, which is why, for example, business fares are much higher from Boston to Reagan National than they are from Providence to Baltimore-Washington International.

Second, these discount airlines do not maintain networks that are easy to use for complicated itineraries or which afford easy access to airports close to smaller cities. They rely on the willingness of a traveler to drive to reach an airport where fares are low. For many travelers, this is an excellent tradeoff, but for a substantial number of business travelers, it is not.

Third, Southwest may be second in the nation in the number of passengers it carries, as some are fond of noting, but it is much smaller in terms of its overall volume of business, which is ultimately how economic impact is measured. Southwest is seventh in the number of Revenue Passenger Miles (the standard measure of output) and even if it grows as rapidly as analysts assure us it will, it will still be responsible for a substantially smaller share of industry total revenue or industry total output than its large network rivals, not to mention the Big Two.

Finally, Southwest itself is not a charitable organization, fully conceding Herb Kelleher's legendary benevolence and charm. Its pricing is constrained by network carriers, just as network carriers constrain it. If the pricing umbrella is set higher by the Big Two, Southwest itself can charge more. Southwest claims that its main competition is the car, but that is only true in the short-haul, point-to-point markets that are no longer the mainstay of its system or the source of its growth. In fact, the car has become much more a complement for travel on Southwest than a substitute. Its customers drive significant distances to get to its uncongested airports. If the Big Two price higher, Southwest can charge more and still make it worthwhile for its customers to drive to its flights. Each rise in Southwest's price level would cost the public a very great deal. Southwest and its brethren are a very valuable part of the U.S. airline system, but its existence is certainly not a substitute for strong competition among network airlines.

In conclusion, this is not just another merger and not just another bailout of a failing airline. The American/United/USAirways transaction is an attempt to undermine the competition created by deregulation. It will do this by building a wall of scarce East Coast infrastructure around a fortress occupied by a Big Two, who will use the protection of that fortress to attack their pursuers. With all its imperfections, deregulated airline competition has served the United States well. The Big Four of the CAB, protected from each other by regulation, is now a group of six highly rivalrous network airlines in which at least three of the smaller players are gaining on the larger two, supplemented and disciplined by a large and growing discount system. Congress and the Administration should not allow those who have the most to lose from this evolution to put a halt to it.

The CHAIRMAN. Thank you very much.

Ms. Hecker.

STATEMENT OF JAYETTA Z. HECKER, DIRECTOR, PHYSICAL INFRASTRUCTURE ISSUES, U.S. GENERAL ACCOUNTING OFFICE

Ms. HECKER. Good morning, Mr. Chairman. I am very pleased to be here.—on your screen?

[Screen.]

The CHAIRMAN. Yes.

Ms. HECKER. I am here representing GAO. We will bring to bear 20 years of work that GAO has been doing following airline deregulation and supporting Congress on the impacts of deregulation.

What I want to do here is three things. These are to focus on some of the data on the actual shifts in competition, that might be a unique contribution. We have not really had that on the table yet. Second, what we think are some of the key elements of the American Airlines proposal; and finally, what the key critical policy issues are.

[Screen.]

Now, on the data, what I have here is a chart that has two scales. On the left is number of markets, on the right are the passengers affected. Then there are three clusters of airline mergers or consolidations. The American Airlines-TWA is on the left, in the middle is the United Airlines-US Airways, and then on the right for comparison purposes is the Northwest Airlines-Continental stock acquisition and alliance that occurred several years ago.

Now, as you see, this is focusing on markets where there would be a decrease of competition. So this is where one of the merging carriers will no longer be an independent competitor. From the American Airlines-TWA agreement, there would be a reduction of competition in 367 city pairs markets, that is from one city origin to a destination. Eleven million passengers traveled in those markets in 1999. I should emphasize, this data is 1999. It is the only complete useful data for doing this kind of analysis. We recognize there may have been some shifts in passengers and markets that occur, but these data are highly sufficient to illustrate orders of magnitude of competitive impacts.

In the middle are the competitive impacts of the United Airlines-US Airways deal. That has 290 markets or city pairs where competition would be reduced; 16 million passengers traveled in those markets.

What is interesting here is the basis of comparison with the competitive effects of the Northwest Airlines-Continental deal. As you see, only 63 markets were affected by that, with 2 million passengers. This was a deal that 2 years ago the Justice Department opposed on the basis of severe constraints on competition. So clearly we are looking at an order of magnitude far more significant and far more pervasive in terms of numbers of markets and numbers of passengers affected.

The CHAIRMAN. Ms. Hecker, what percent of the market do both of those represent on the left, roughly?

Ms. HECKER. The universe of markets here is 5,000 markets. About 330 million passengers traveled in those markets in 1999. So 11 million is not a massive share, but it is on those markets, obviously.

In addition, we actually can give you the number of markets—it is kind of a subset of this—not just where competition is reduced, but where the new merging carriers would become dominant. Of the 367 markets in which the American-TWA merger would decrease competition, the merged carriers would dominate 161. So in a little less than half of the 367 markets, the new American-TWA would have over a 50 percent share in those markets and that would affect almost 5 million passengers. The United agreement would decrease competition in 290 markets, and the new carrier would have domination, over a 50 percent share of the market—in 126.

[Screen.]

Now again, what I want to do, though, is turn to the fact that there are some increases in competition that result from these mergers. DOT defines an effective competitor as a carrier that has at least 10 percent of the market. So these markets are where, for example in the American-TWA example, each of the carriers had less than a 10 percent share, so they were not really an effective competitor in 1999, and by joining, there would be 150 markets where American and TWA combined would be a more effective competitor. As you see, there are quite a number of passengers in those 150 markets, affecting 15 million passengers.

The United Airlines-US Airways deal has 65 markets where there would be an increase in competition, affecting 2.9 million passengers. Interestingly, again the comparison with the Northwest-Continental deal is very informative and enlightening. You see massive increases in competition from that deal, and yet it did not pass DOJ muster.

Now, just to go back to the prior slide, from the American deal we are looking at decreases in competition in 367 markets, increases in 150 markets.

The second point I wanted to share was what we think are the really key issues raised by the American proposal. I think, as several people have said here, one of the most important things to do is recognize the distinct elements of the American Airlines proposal. TWA is a separate proposal and we are very pleased to hear that it is entirely separate and not contingent on the aspects of the agreement that relate to United Airlines.

TWA clearly is in severe financial straits. Even though a significant number of markets may be affected, those are markets that would otherwise lose the service, and the antitrust laws provide a very different perspective for a failed firm. So there are less anticompetitive effects that are raised by the part of the American agreement with TWA and clearly present more benefits, many of which you have heard today from the various speakers.

The parts of the agreement that raise the most significant issues—and I think you have begun to hear some of those—are the elements of the agreement that have to do with the unique and distinct arrangements with United Airlines, the new United Airlines. There are three areas that you see we have highlighted: the sharing of the shuttle, 50 percent; acquiring the 49 percent share of DC Air; and agreeing to compete at select US Airways hubs.

The key question is how competition would be affected by these agreements—that is, whether you would get vigorous, effective competition between these two major massive carriers that probably cannot be matched by any subsequent merger or whether it may signal some period of cooperation and recognition of mutual interdependence. That is a well-established theory in economics that has empirical evidence, that when there are few firms in a market and they meet in many markets, in this case 1106 markets in which the new United and the new American would meet, they quickly recognize their mutual interdependence and compete less vigorously.

I think that is one of the factors that one would clearly want to take into account in terms of what kind of competition might occur given some of these transfers.

I also want to highlight a provision of the agreement that has not been researched or discussed, but would appear to be extraordinarily unusual. It basically continues a tied relationship between United and American. This is not an agreement where American buys some assets from United and they each go their own way and then compete using those assets. There is a provision in this agreement that basically ties American not to grow more than 7.5 percent. If American grows, if they enter into an agreement with another major carrier that would have them grow bigger than that, United can take back the shuttle and undo every bit of the assets that they have transferred to them.

This deal would be in effect for 4 years and it is an extraordinary agreement, something that we have never seen. The experienced people in the field we have talked to have also never seen such a unique agreement.

This brings me to the last point, which is basically a framing of the larger issue. So we hone in on what we think are the critical issues of the American proposal and its relationship to United, which relate to the fundamental restructuring that is represented by these proposals. There are three issues that we think are critical.

The first one I have already alluded to, that is the extent to which there would be vigorous competition between American and United. We think the unique nature of this arrangement and the interdependence of the airlines would be very apparent and we think this raises some serious questions that Congress and clearly the Department of Justice would be wise to further explore.

The second is not really second in my view. I think you have heard it somewhat before. The cornerstone of effective competition in any industry is open access. That is the source of lifeblood for competition, particularly if you have a relatively concentrated industry. Barriers to entry in this industry already exist. They are significant and they are already impeding the entry of new carriers, as we can see by the pending Justice Department complaint against American's behavior in Dallas-Fort Worth against three new low-cost carriers.

So barriers to entry already exist. I cannot tell you how much they might increase or ways they might increase by these broad consolidation areas, but it is probably the single most important factor to understand, combined with the first one. It is also important that if you are going to have 50 percent of the market, two huge carriers are not competing. But in essence, this really combines with the second point, because if the two huge carriers are not competing and recognize their interdependence, their assets could potentially be used collectively to impede further entry.

My final point is one that I know is of interest to many members of this Committee, the Congress and the flying public, and that is what happens to small community service. It is very important. It has been well documented that the benefits of deregulation have not been experienced equally by smaller communities. We are actually doing some work right now for Senator Snowe looking at the placement of regional jets and how that has been affecting small communities.

Overall, small community service remains a very important equity issue in deregulation. The core question really is whether small communities are better off in the hands of a concentrated, highly networked community which perhaps promises tremendous interlining—where you can be in the smallest city, but if there is service in your town, then you can get anywhere in the world on line, and not have to change carriers. That is one of the big benefits United and American outline as a benefit of their plans for communities—that you do not have to change planes, you can be on us everywhere in the world. So that is one side of it, saying that you are better off going with that kind of concentration and vast interconnected global networks.

Or are you better off putting your hat in with a more competitive industry? I think you have heard Ms. Slaughter's answer about that. There is a different view on this and I think that is one of the fundamental assessments needed at the end of the day to evaluate the direction of industry consolidation.

I appreciate the opportunity to be here and put some of these issues on the table and would be pleased to take any questions. Thank you, Mr. Chairman and Members of the Committee.

[The prepared statement of Ms. Hecker follows:]

PREPARED STATEMENT OF JAYETTA Z. HECKER, DIRECTOR, PHYSICAL INFRASTRUCTURE ISSUES, U.S. GENERAL ACCOUNTING OFFICE

Mr. Chairman and Members of the Committee:

We appreciate the opportunity to testify on the potential implications of merger proposals recently announced by major airlines. In May 2000, United Airlines (United) proposed to acquire US Airways and divest part of those assets to create a new airline to be called DC Air. More recently, American Airlines (American) has proposed to purchase Trans World Airlines (TWA), along with certain assets from United. These proposals have raised questions about how such consolidation within the airline industry could affect competition in general and consumers in particular.

Extensive research and the experience of millions of Americans underscore the benefits that have flowed to most consumers from the 1978 deregulation of the airline industry, including dramatic reductions in fares and expansion of service. These benefits are largely attributable to increased competition—by the entry of both new airlines into the industry and established airlines into new markets. At the same time, however, airline deregulation has not benefited everyone; some communities have suffered from relatively high airfares and a loss of service due in part to a lack of competition. GAO has been analyzing aviation competition issues since enactment of the Airline Deregulation Act. Our work over the last decade has focused on challenges to competition and industry performance, including various mergers, the Department of Transportation's (DOT) role, concentration in select airports, key airline operating and marketing practices, barriers to entry, small community service, and fares in dominated markets.[1]

The potential shifts in industry structure that would be brought about from the proposed mergers represent a crossroads for the structure of the airline industry and the state of competition and industry performance.[2] These proposed mergers raise numerous public policy issues that require reasoned responses. Ultimately, the Department of Justice (DOJ) has the primary responsibility to evaluate these mergers. In its review, Justice considers a number of factors, including increases in market concentration; potential adverse effects on competition; the likelihood of new entry; possible efficiencies or other benefits; whether one of the airlines would fail and exit the market if the merger failed to occur; and whether a less anticompetitive alternative exists.

We recently issued a report on the potential effects of the proposed merger between United and US Airways.[3] That review, using the most recently available data from DOT on the top 5,000 domestic airline markets, generally focused on changes in market structures and not on other issues that DOJ might take in consideration.[4] Our statement today is based on that report and our earlier work on airline competition issues, along with initial analyses of the potential effects of the various proposed transactions between American, TWA, United, and US Airways. We will: (1) present an overview of potential shifts in industry structure and markets associated with both the American and United proposals; (2) identify key issues associated with American's proposed transactions; and (3) identify some critical public policy issues associated with the potential consolidation in the industry.

In summary:

- If both the United-US Airways merger and American-TWA acquisition are consummated, new United would have the largest market share of any U.S. carrier—over 27 percent—and new American would have a 22.6 percent share. Each proposal could have both harmful and beneficial effects on consumers. The United and American proposals would each reduce competition in approximately 300 markets, with each affecting over 10 million passengers. Each proposal would allow the new larger carrier to dominate (i.e., obtain a greater than 50-percent market share) more than 100 new markets. However, the mergers would also each create new competitors where, previously, each of the merging carriers had less than a 10-percent market share. Each would provide other benefits to consumers as well, such as creating new online service in certain markets and possible new routings allowing passengers to connect over different cities.

- American's proposed arrangements with TWA, United, US Airways, and DC Air raise a number of significant questions that cannot be answered now, in part because many of the details of these arrangements are still unknown. Although TWA has been in poor financial condition for years, the question remains whether American's purchase of TWA represents the least anticompetitive means to preserve its assets. Other questions arise about how the agreements that American has tentatively made with United (regarding the future of the US Airways Shuttle between Washington, New York, and Boston and the assets associated with the proposed DC Air) would affect competition.

- The consolidation in the industry that might result from both the proposed American and United transactions raises major public policy issues. These include, but are not limited to, questions about how a more consolidated industry might further raise barriers to market entry by new airlines, how the two merged airlines might compete in key markets, whether the merged carriers

[1] See list of related GAO products attached to this statement.

[2] Technically, American has proposed to acquire the assets of TWA, which declared bankruptcy. For presentation purposes in this statement, however, we will refer to the transaction as a merger.

[3] *Aviation Competition: Issues Related to the Proposed United Airlines—US Airways Merger* (GAO–01–212, Dec. 15, 2000).

[4] We analyzed the most recent data available from DOT on the top 5,000 city-pair markets, which covered calendar year 1999. For this statement, we applied the same methodology, using the same data, as we did in our December 2000 report on the proposed United-US Airways merger. We recognize that competition or service in particular markets is likely to change over time with the entry or exit of different carriers. Carriers may add or reduce service in markets. These data illustrate the approximate orders of magnitude of the various transactions. We have not subtracted passengers or markets that may be affected by DC Air markets or the proposed agreement between United and American to share the current US Airways shuttle from the data for new United.

would expose the public to greater risks of travel disruptions, and how service to small communities might be affected.

Background

On May 24, 2000, United and US Airways agreed to merge their operations. Under the terms of the proposed merger, United would acquire US Airways in a transaction valued at $11.6 billion. Specifically, United would pay $60 for each share of common US Airways stock for a total of $4.3 billion and would assume $1.5 billion in US Airways net debt and $5.8 billion in aircraft operating leases. According to information from United, the combined company ("new United") would have approximately 145,000 employees. It would operate eight hubs in six states and serve a total of 380 airports throughout the country, reaching communities in every state.

Under the terms of the proposed merger, United plans to divest some of the assets US Airways possesses at Ronald Reagan Washington National Airport (Reagan National). These assets would be used to create a new airline known as DC Air. They include 222 departure and arrival slots,[5] several gates and related airport facilities, and the operations of an existing commuter airline.

In January 2001, American proposed acquiring TWA (which declared bankruptcy) for approximately $3.5 billion, including $500 million in cash, $3.0 billion in estimated lease assumptions, and $200 million in other financing. In addition, American also announced that it had agreed with United to purchase certain assets from United and US Airways, including half of the US Airways Shuttle between Washington, New York, and Boston, and a 49-percent share of DC Air. According to information from American, the combined company ("new American") would have approximately 120,000 employees. It would operate five hubs, nearly 1,000 aircraft, and gain a large number of slot and gate resources at key airports in the eastern United States.

The consummation of the proposed mergers are subject to approvals by various regulatory bodies. Both DOJ and DOT have responsibilities for reviewing airline mergers and acquisitions.[6] DOJ has the authority to review mergers or stock acquisitions before they take place to determine whether they violate antitrust laws. Under the Hart-Scott-Rodino Act, an acquisition of voting securities above a set monetary amount must be reported to DOJ for prior review. DOJ has the authority to institute judicial proceedings under the Clayton Act if it determines that a merger or acquisition may substantially lessen competition in a relevant market or if it tends to create a monopoly.[7] If DOJ believes any agreement is anticompetitive in whole or in part, it may seek to block the agreement in federal court. TWA's bankruptcy proceeding is now before the U.S. Bankruptcy Court for the District of Delaware. DOT conducts its own analysis of airline mergers and acquisitions and submits its views and any relevant information it has to DOJ. In addition, when transactions involve the transfer of international route authority, DOT is responsible for approving such matters to ensure that they are consistent with the public interest.

Highlights of Potential Changes in Industry Structure

Although the proposed acquisition of TWA by American would not affect as many passengers as the merger between United and US Airways, the transaction itself has the potential for preserving assets in the market. If both the United-US Airways merger and the American-TWA acquisition are consummated, new United would have the largest market share of any U.S. carrier—27.2 percent—and new American would have a 22.6 percent share (based on revenue passenger miles, a recognized measure of airline size[8]). Thus, if both transactions are consummated,

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[5] The Federal Aviation Administration limits the number of operations (takeoffs and landings) that can occur during certain periods of the day at four congested airports—O'Hare in Chicago; Reagan National in Washington, D.C.; and Kennedy and LaGuardia in New York. The authority to conduct a single operation during these periods at these four airports is commonly referred to as a "slot."

[6] The merger may also be reviewed by the European Commission and state attorneys general.

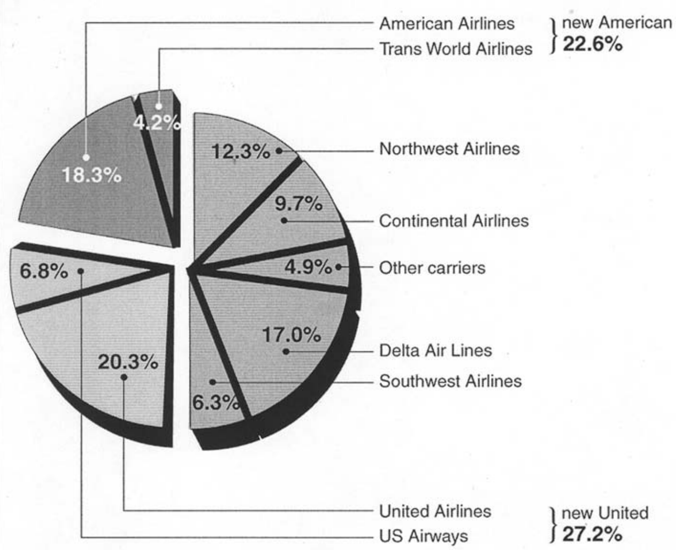
[7] Justice's Horizontal Merger Guidelines (United States Department of Justice and Federal Trade Commission Revision to the Horizontal Merger Guidelines (Apr. 8, 1997)) describe the process used to analyze the potential effect of a merger under the Clayton Act. Under the Hart-Scott-Rodino Act, an acquisition of voting securities above a set monetary amount must be reported to Justice for prior review. Justice has the authority to institute judicial proceedings under the Clayton Act if it determines that a merger or acquisition may substantially lessen competition in a relevant market or if it tends to create a monopoly.

[8] These percentages do not take into account the market share that might be attributable to DC Air or the sharing of the US Airways Shuttle. Revenue passenger miles represent the number of paying passengers transported over each mile. "Revenue passengers" do not include those

Continued

new United and new American would together control nearly 50 percent of total airline traffic. Many industry analysts observe that these measures would likely not be the end of the movement toward further industry consolidation. Figure 1 compares the percentage share of total revenue passenger miles that new American and new United would carry relative to that flown by other major U.S. airlines. Appendix I shows the relative size of major U.S. passenger airlines as indicated by common measures of airline market presence, along with the airlines' 1999 total operating revenue.

Figure 1: New American and New United Would Have Nearly 50 Percent of Total U.S. Domestic and International Passenger Travel



Note: Percentages may not total due to rounding.

Source: GAO's analysis of data from DOT for the 12 months ending June 30, 2000.

American's acquisition of TWA would reduce competition in 367 markets—more than the 290 markets in which competition would be reduced from the proposed merger between United and US Airways.[9] The number of passengers potentially affected by the new American restructuring would be 11 million, compared to the 16 million potentially affected by new United. New American would also have a larger increase in the number of markets they could dominate (161) compared to United (126). However, the dominated markets associated with the proposed American-TWA arrangement affect fewer passengers than those dominated markets associated with the proposed United-US Airways merger (4.9 million compared to 6.9 million). The total number of markets that new American would dominate would be 552 compared with 1,156 that new United would dominate. On the other hand, new American would increase competition in more markets than new United (150 compared to 65), potentially benefiting more than five times as many passengers (15.4 million compared to 2.9 million).

As a frame of reference for analyzing the competitive significance of the proposed mergers, we compared them with our analysis of the proposal in 1998 by Northwest to acquire a majority of the voting stock in, and enter into an alliance with, Conti-

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who are flying on frequent flyer award tickets and others who did not pay for their flights (e.g., airline employees).

[9] As we did in our December 2000 report on the proposed United-US Airways merger, we define a market as a city-pair. We define a competitor as an airline that had at least a 10 percent share of the passenger traffic in that market, based on DOT's 1999 data on the top 5,000 city-pair markets, which was the most currently available at the time of our analysis.

nental.[10] The potential number of markets and passengers who might be adversely affected by either the proposed United-US Airways or American-TWA mergers are much greater than those that might have been affected by the Northwest-Continental stock acquisition and alliance. The number of passengers who could benefit from the American-TWA merger is roughly comparable to those who could have benefited from the Northwest-Continental stock acquisition and alliance. Table 1 summarizes the number of markets and passengers affected by the proposed mergers and compares them to the markets and passengers that potentially would have been affected by the Northwest-Continental stock acquisition and alliance.

Table 1: Comparison of Potential Competitive Impact of the Proposed United-US Airways and American-TWA Mergers with the Proposed Northwest—Continental Stock Acquisition and Alliance

	American-TWA (1999 data)		United-US Airways (1999 data)		Northwest-Continental (1997 data)	
Competitive Factor	Numbers of markets	Passengers affected (millions)	Numbers of markets	Passengers affected (millions)	Numbers of markets	Passengers affected (millions)
Markets where competition would decline	367	11	290	16.0	63	2.0
Newly dominated markets	161	4.9	126	6.9	25	2.4
Total dominated markets	552	27.5	1,156	61.1	492	40.7
Markets where competition would increase	150	15.4	65	2.9	286	15.1

Source: GAO's analysis.

If both mergers proceed, the two new carriers would both compete in 1,106 of the top 5,000 markets. Competition could be reduced in 267 of those markets where, in 1999, about 10.3 million passengers traveled. That is, in 267 markets, as a result of combining what are now separate competitors (i.e., each airline had at least a 10 percent share of the market) through their proposed merger, one competitor would no longer exist. However, the data net out markets where the merger might create a new effective competitor (i.e., where the two merging carriers previously had less than a 10-percent market share but combined have over 10 percent.) Table 2 shows the number of markets and passengers that could potentially be affected by reduced competition due to the combined effect of the two mergers.

[10] Northwest proposed to acquire a majority of the voting stock in, and enter into an alliance with, Continental. Northwest and Continental announced in January 1998 that Northwest was to acquire 8.7 million shares of Continental's stock. These shares gave Northwest 51 percent of the voting rights in Continental. In addition, the two airlines were entering into an alliance that would connect their route systems. A variety of industry analysts told us they believed that Northwest and Continental would not act as independent competitors over the long run. As a result, our analysis of the potential competitive effects of the stock acquisition and alliance assumed that Northwest and Continental would behave as though they had merged. See *Aviation Competition: Effects on Consumers From Domestic Alliances Vary* (GAO/RCED–99–37, Jan. 15, 1999). Our analysis here largely parallels our analysis of the Northwest-Continental stock acquisition and alliance.

DOJ announced a tentative settlement in its antitrust suit opposing Northwest's purchase of a controlling interest in Continental on November 6, 2000. Under the terms of the agreement in principle, Northwest would divest all but 7 percent of the voting interest in Continental and would be subject to significant restrictions on its ability to vote any stock it retains.

Table 2: Markets Where New American and New United Would Meet and Competition Could Be Reduced

Change in the number of competitors	Markets	Passengers (millions)
From 3 to 2	64	2.6
From 4 to 3	123	3.5
From 5 to 3	3	0.1
From 5 to 4	69	3.7
From 6 to 5	8	0.4
Total	267	10.3

Source: GAO's analysis of data from DOT.

Thus, in 64 of the 267 markets, the two proposed mergers leave new United and new American as the only remaining competitors. In 1999, about 2.6 million passengers traveled in those 64 markets. In 126 markets where 3.6 million passengers traveled in 1999, new United and new American would be two of only three remaining competitors.

Conversely, the proposed United-US Airways and American-TWA mergers would also benefit consumers. In markets where one of the two merging airlines now has limited market shares, the merger would allow them to create competition against other airlines. For example, were both mergers approved, approximately 7 million passengers could benefit from gaining an additional competitor in 107 markets. Additionally, by extending the carriers' operations to city-pairs where only one of the two airlines previously operated at each endpoint, the merger would create new on-line service between those communities.[11] Finally, the merger would benefit members of each airline's frequent flyer programs by expanding the number of destinations that the members could reach. The airlines also assert that the proposed mergers would deliver other benefits. For example, American and TWA passengers may benefit by being able to connect to their destination over different hubs.

Proposed Arrangements Between American, TWA, United, US Airways, and DC Air Raise Significant Competition and Service Issues

American's acquisition of TWA and its purchase of certain assets of United and US Airways, including a portion of DC Air need to be discussed separately, as the implications would seem to be quite different. Each component of American's proposed transactions raise numerous questions.

Does American's purchase represent the "least anticompetitive" means to preserve the presence of TWA's assets in the market? By many accounts, TWA has been in a difficult financial position for years. Since 1992, TWA has entered bankruptcy three times. It has failed to earn an annual profit during the past 12 years. Regardless of whether TWA ceases operating entirely because of its financial failure, or whether TWA is purchased by another airline, an independent competitive presence in the 103 cities that the airline serves will be lost. (However, were TWA to cease operating entirely, the loss of service would likely be temporary, as the market would adjust to meet the demand for travel.)

Whether the loss of competition from TWA is a positive or negative development depends on a number of factors. DOJ will have to review many of those factors, including increases in market concentration, potential adverse effects on competition of the transaction, possible efficiencies or other benefits, and the likelihood of new entry. It is also DOJ's responsibility to determine whether, for example, absent the merger, TWA's assets would exit the market if it failed, and whether there is no less anticompetitive alternative. On the one hand, we recognize that there are many important considerations involved with preventing TWA from ceasing operations entirely, such as continuing service to markets and maintaining jobs for its employees. On the other hand, the question exists about how the loss of TWA's competitive presence could be mitigated. For purposes of creating more competition in the U.S. domestic aviation market, would it be better if an airline other than American bought TWA?

American's purchase of certain assets of United and US Airways, including a portion of DC Air, raises other significant questions about how competition may be af-

[11] On-line service provides passengers with connecting flights without requiring them to change airlines. Service that requires passengers to change airlines to continue their flights (excluding those requiring a passenger to transfer between a larger airline and its commuter affiliate or other airlines with which it may have a code-sharing agreement) is referred to as "interline" service.

fected. Several issues appear central to an assessment of possible anticompetitive impacts of the proposed transactions:

How would American's purchasing part of DC Air affect competition? As DC Air was originally conceived in the proposed merger between United and US Airways, questions arose about whether it would be an independent competitor, particularly in certain key markets relative to new United. If American purchases 49 percent of DC Air, passengers who fly on DC Air could earn American rather than United frequent flyer miles. Passengers who may be flying beyond Washington, D.C., could connect with online service onto other American flights rather than on flights operated by United. American's purchase of part of DC Air means that American, not United, would provide some of the aircraft, crew, and other support to DC Air.

How might American's purchasing part of DC Air affect service to DC Air's markets? Under the original proposal to create DC Air, the airline was to serve 44 markets out of Reagan National, most of which are now served by US Airways. DC Air had expressed a commitment to maintain service to essentially all of those cities, using the 222 arrival and departure slots that it would obtain as part of the US Airways divestiture. We do not know what commitment, if any, American expressed regarding maintaining that service. We also do not know what agreements, if any, American made with DC Air to buy the remaining 51 percent interest in the company or whether American will use the slots at Reagan National for other markets.

How would American's sharing shuttle operations with United alter competition? American and United have proposed forming a joint venture to share the operations of the US Airways shuttle at New York LaGuardia, Boston, and Washington Reagan National for at least 20 years. The two airlines expect to coordinate schedules, ticketing, frequent flyer programs, and access to passenger lounges. We do not yet know how this arrangement might affect price competition in the market.

Does American's adding flights in certain United-US Airways hub routes enhance competition? As part of the agreement with United, American has agreed to provide at least two daily flights on five routes for 10 years. Four of those markets—between Chicago O'Hare and Charlotte, Los Angeles and Philadelphia, San Jose and Philadelphia, and Washington and Pittsburgh—complement American's existing network by originating in one of the airline's "focus cities." However, we do not know what impact the agreement between American and United will have on competition between the two airlines on price and service in those markets.

Critical Public Policy Issues Associated With the Industry's Possible Consolidation

Some industry observers have suggested that the American and United proposals mark the beginning of a new wave of transition. Any industry consolidation that these proposals bring about raises a number of important public policy issues for consideration. We highlight some of these issues—relating to market entry, competition among the newly merged airlines in key markets, potential travel disruption, and service to small communities—while recognizing that many others also exist.

What barriers to market entry might the proposed mergers exert? Scores of new airlines have begun commercial passenger service since the deregulation of the industry. Although most failed, other airlines have managed to compete, and some have done so quite profitably. The most notable example, of course, is Southwest. Others—such as ATA, AirTran, and JetBlue—have also experienced success so far. The success of airline deregulation in leading to lower fares and better service stems in part from competition spurred by the entry of new airlines, i.e., low fare carriers are recognized as providing the primary fare discipline in the marketplace. A January 2001 DOT report on exclusionary practices concluded that major airlines have the opportunity and the means to protect their market power by frustrating new entry. DOT found there had been instances in which incumbents drove new entrants out of markets by cutting fares and flooding the market with capacity. Once the new entrant was driven out of the market, the incumbent sought an increase in fares and reductions in service.

If American and United fly nearly half of the industry's traffic, a key issue that policy makers would need to address is whether new low-cost carriers would be able to enter markets and compete. Because established carriers would control vast numbers of facilities (including slots and gates) at key airports, would those new carriers be able to offer service in major markets? Would American and United's sales and marketing efforts (such as their frequent flyer programs and code-sharing affiliations such as the Star Alliance and OneWorld) present barriers that would be too great for new entrants to overcome? How effectively would those new carriers compete if the American and United transactions spurred additional consolidation in the industry, possibly raising entry barriers even higher?

Would the transactions between American and United alter how they would compete in key markets? The proposed United and American arrangements—including the agreements in which American would share the US Airways shuttle with United and compete in certain markets between United and US Airways hubs—raise questions regarding the extent to which the carriers might compete vigorously. Economic literature and empirical evidence indicate that when fewer firms exist in a market and those firms meet in many markets (e.g., city-pairs), they are likely to recognize their interdependence and compete less vigorously.

To identify the orders of magnitude of markets that might be affected by new United and new American, we examined the number of markets where the merged carriers would compete against each other.[12] New American would be a competitor in over 2,100 of the top 5,000 markets, while new United would compete in over 2,900. The new carriers would both be competitors in 1,106 markets. Table 3 summarizes the combined passenger shares of the two carriers in these markets.

Table 3: Passenger Shares of New United and New American in Markets Where Carriers Would Both Operate

Combined passenger share of new United and new American	Markets	Percent
81–100%	286	25.9
61–80	324	29.3
41–61	323	29.2
20–40	173	15.6
TOTAL	1,106	100.0

Source: GAO's analysis of 1999 data from DOT.

In 610 of the 1,106 markets (or about 55 percent), the two carriers would account for over 60 percent of the traffic. To the extent the two large carriers recognize their interdependence in these and the other 496 markets where they would both operate, should the carriers not compete vigorously, it could adversely affect fares and service.

Will the public be exposed to greater risk of travel disruptions, in light of the merged carriers' breadth of service? We have witnessed three relatively recent examples of how carriers' labor difficulties can greatly disrupt travel: American's 1997 disruption following its purchase of Reno Air, United's difficulties this past summer, and Delta's current challenges with its pilots. Other labor groups' contracts with the airlines are also coming up for renewal in the near future. If the proposed mergers are approved, and either airline encounters major labor problems, how severely could the public's travel be disrupted? The aviation system has relatively little unused capacity in it now, having been operating at or near record load levels for some time. In general, could the significant integration challenges (not only labor, but also systems and fleets) presented by the American and United proposals make the public more vulnerable to network wide disruptions?

How might a consolidated industry affect service to small communities? The quality of air service to smaller communities and the fares that passengers in those communities pay relative to those paid in larger communities have been issues that the Congress has been concerned about for some time. At the same time, one of the benefits of airline mergers and alliances has been the ability of the larger carrier to provide online service to increased numbers of destinations. For example, the United-US Airways merger could improve competition and service in 256 relatively small markets by providing new online connections. The airlines have also claimed that small communities would gain greater access to international markets through their global alliances. However, the mergers could erode service to many small communities where the merging airlines compete, even if the service provided is over different hubs. One analyst suggested, for example, that American might discontinue TWA's current turboprop service between Bloomington (Illinois) and St. Louis, because American also serves Bloomington, but uses small jet aircraft to and

[12] As noted earlier, in this and previous reports, we defined a competitor as an airline that carried at least 10 percent of the passenger traffic in a given market. This is the same definition used by DOT.

from Chicago. Would a more dispersed and competitive market structure offer better promise of providing affordable air access for small and medium sized communities to major US business centers? How might the potential effect of industry consolidation on new entry affect small and medium sized communities?

Conclusions

There are a number of unanswered questions that the Congress, DOJ, and DOT need to address in evaluating the proposed mergers. The proposals by American, TWA, United, US Airways, and DC Air constitute the most significant recent changes that have occurred in the airline industry, and the outcome of these decisions could have both positive and negative effects for consumers for years to come.

This concludes my statement. I would be pleased to answer any questions you or other Members of the Committee might have.

JAYETTA Z. HECKER,
Director, Physical Infrastructure Issues.

Appendix I

Combined Domestic and International Measures of Airline Size, 12 Months Ending June 30, 2000

Airline	Revenue passenger enplanements [a]		Revenue passenger miles		Total operating revenue	
	Number in thousands	Percent of total	Number in thousands	Percent of total	Dollars in millions	Percent of total
Delta Air Lines	106,218,000	18.8	106,849,814	17.0	14,711	16.3
United Airlines [b]	87,113,000	15.4	127,455,682	20.3	18,027	20.0
American Airlines [c]	85,400,000	15.1	114,832,223	18.3	17,730	19.6
Southwest Airlines [d]	69,056,000	12.2	39,641,182	6.3	4,736	5.2
US Airways [e]	56,417,000	10.0	42,898,817	6.8	8,595	9.5
Northwest Airlines	56,003,000	9.9	77,324,776	12.3	10,276	11.4
Continental Airlines	44,868,000	7.9	60,980,078	9.7	8,639	9.6
Trans World Airlines	26,271,000	4.7	26,650,717	4.2	3,309	3.7
America West Airlines [f]	19,523,000	3.5	18,558,027	3.0	2,211	2.4
Alaska Airlines [g]	13,694,000	2.4	11,962,007	1.9	2,082	2.3
Total [h]	564,563,000	100.0	627,153,323	100.0	90,316	100.0
New United [i]	143,530,000	25.4	170,354,499	27.2	26,622	29.5
New American [i]	111,671,000	19.8	141,482,940	22.6	21,039	23.3

[a] "Passenger enplanements" represent the total number of passengers boarding an aircraft. Thus, for example, a passenger that must make a single connection between his or her origin and destination counts as two enplaned passengers because he or she boarded two separate flights.

[b] Total operating revenues are for the parent (UAL Corporation).

[c] Total operating revenues are for the parent (AMR Corporation).

[d] Southwest Airlines provides only domestic service.

[e] Total operating revenues are for the parent (US Airways Group, Inc.).

[f] Total operating revenues are for the parent (America West Holdings, Inc.).

[g] Total operating revenues are for the parent (Alaska Air Group, Inc.).

[h] Totals may not add to 100 percent due to rounding.

[i] Totals for new United and new American do not make any allowance for those operations that might become part of DC Air or sharing the US Airways Shuttle.

Sources: GAO's analysis of DOT data.

Related GAO Products

Aviation Competition: Issues Related to the Proposed United Airlines-US Airways Merger (GAO–01–212, Dec. 15, 2000).
Reagan National Airport: Capacity to Handle Additional Flights and Effect on Other Area Airports (GAO/RCED–99–234, Sept. 17, 1999).
Aviation Competition: Effects on Consumers From Domestic Alliances Vary (GAO/RCED–99–37, Jan. 15, 1999).
Aviation Competition: Proposed Domestic Airline Alliances Raise Serious Issues (GAO/T–RCED–98–215, June 4, 1998).
Domestic Aviation: Service Problems and Limited Competition Continue in Some Markets (GAO/T–RCED–98–176, Apr. 23, 1998).
Aviation Competition: International Aviation Alliances and the Influence of Airline Marketing Practices (GAO/T–RCED–98–131, Mar. 19, 1998).
Airline Competition: Barriers to Entry Continue in Some Domestic Markets (GAO/T–RCED–98–112, Mar. 5, 1998).
Domestic Aviation: Barriers Continue to Limit Competition (GAO/T–RCED–98–32, Oct. 28, 1997).
Airline Deregulation: Addressing the Air Service Problems of Some Communities (GAO/T–RCED–97–187, June 25, 1997).
International Aviation: Competition Issues in the U.S.–U.K. Market (GAO/T–RCED–97–103, June 4, 1997).
Domestic Aviation: Barriers to Entry Continue to Limit Benefits of Airline Deregulation (GAO/T–RCED–97–120, May 13, 1997).
Airline Deregulation: Barriers to Entry Continue to Limit Competition in Several Key Domestic Markets (GAO/RCED–97–4, Oct. 18, 1996).
Domestic Aviation: Changes in Airfares, Service, and Safety Since Airline Deregulation (GAO/T–RCED–96–126, Apr. 25, 1996).
Airline Deregulation: Changes in Airfares, Service, and Safety at Small, Medium-Sized, and Large Communities (GAO/RCED–96–79, Apr. 19, 1996).
International Aviation: Airline Alliances Produce Benefits, but Effect on Competition Is Uncertain (GAO/RCED–95–99, Apr. 6, 1995).
Airline Competition: Higher Fares and Less Competition Continue at Concentrated Airports (GAO/RCED–93–171, July 15, 1993).
Computer Reservation Systems: Action Needed to Better Monitor the CRS Industry and Eliminate CRS Biases (GAO/RCED–92–130, Mar. 20, 1992).
Airline Competition: Effects of Airline Market Concentration and Barriers to Entry on Airfares (GAO/RCED–91–101, Apr. 26, 1991).
Airline Competition: Industry Operating and Marketing Practices Limit Market Entry (GAO/RCED–90–147, Aug. 29, 1990).
Airline Competition: Higher Fares and Reduced Competition at Concentrated Airports (GAO/RCED–90–102, July 11, 1990).
Airline Deregulation: Barriers to Competition in the Airline Industry (GAO/T–RCED–89–65, Sept. 20, 1989).
Airline Competition: Fare and Service Changes at St. Louis Since the TWA-Ozark Merger (GAO/RCED–88–217BR, Sept. 21, 1988).
Competition in the Airline Computerized Reservation Systems (GAO/T–RCED–88–62, Sept. 14, 1988).
Airline Competition: Impact of Computerized Reservation Systems (GAO/RCED–86–74, May 9, 1986).
Airline Takeoff and Landing Slots: Department of Transportation's Slot Allocation Rule (GAO/RCED–86–92, Jan. 31, 1986).
Deregulation: Increased Competition Is Making Airlines More Efficient and Responsive to Consumers (GAO/RCED–86–26, Nov. 6, 1985).

The CHAIRMAN. Thank you, Ms. Hecker.

I believe that this has been a very important and beneficial hearing and one that has been very educational to all of us. Let us jump right into it, Mr. Carty, to what Ms. Hecker describes as an extraordinary agreement, that if you grow more than 7.5 percent they will take back your assets. What is that all about?

Mr. CARTY. I think that is all about United being concerned they do a transaction with us and we would embarrass them by doing another transaction that would make us dramatically bigger than them. We would be delighted if that was removed, I can assure you. On that particular item, we are the furthest thing from conspirators that you can imagine. United and we fought vigorously over this contract, I can assure you.

United did not offer, as Mike suggested, to give us half the shuttle. Just as they insisted on the provision you just alluded to, we insisted we would not do a transaction with them unless we had half the shuttle. This was a very vigorous negotiation between two longstanding and very vigorous competitors that, I might add that Jim Wilding, who is the President of the Metropolitan Washington Airports Authority, recently referred to as the cobra and the mongoose. That has been the history of American and United and I can assure you it will continue to be the history of American and United.

The CHAIRMAN. Well, because it was a hard-fought agreement, you entered into one of the most extraordinary agreements in history?

Mr. CARTY. As I say, we would be delighted to have that removed.

The CHAIRMAN. I do not quite understand that.

Mr. CARTY. Well, certainly, Senator, as I testified, there are a lot of aspects of this agreement that work very well for American. There are a lot of aspects of this agreement that provide competitive remedies to the issues raised by Justice.

United did not dream up an idea of enhancing their major competitor. If there was a conspiracy here, I think you would have to conclude that the Department of Justice was part of it, because United was clearly responding to issues that the Department of Justice raised with them. As I said in my testimony, this Committee and the Justice Department will have to decide whether those remedies are sufficient. But clearly, the provisions of this contract were a response to the Department of Justice.

The CHAIRMAN. According to GAO's analysis, the newly merged United and American Airlines would control a combined 60 to 100 percent of the passenger traffic in more than 55 percent of the markets where both would compete, which works out to 610 markets. You testified that you are worried about a United-Delta duopoly in the shuttle market. Yet why should not consumers be alarmed that the two mega-airlines will have effective duopolies throughout the country?

Mr. CARTY. I have not, Mr. Chairman, reviewed the GAO study to determine which precise markets they are talking about. There is a distinction in the shuttle markets, as you well know——

The CHAIRMAN. Let us say there is a duopoly in only one market. Would that concern you?

Mr. CARTY. What I was about to say, Mr. Chairman, is there is a distinction in a market that cannot be entered as a consequence of slots, and the shuttle markets are such markets. We have had entry and exit from a vast array of markets in this market where we are not confined, as Mr. Leonard has suggested, by the absence of slots. The shuttle markets are a market that we would long since have entered unilaterally as a third competitor had there been slots available to us.

I know you and this Committee have been concerned about that issue for many years. We continue to be concerned about it. On one area we would agree absolutely with Mr. Leonard and that is the faster we can move in this country to remove the limitations that are imposed by the limitations of the air traffic control system, the happier all of us will be.

The CHAIRMAN. Mr. Johnson stated that the combination of DC Air with the support of American will become the largest presence at Reagan National. Is American going to compete against DC Air, a carrier that it owns 49 percent of?

Mr. CARTY. I think it is fair to say, Mr. Chairman, our intent is to run a complementary system with Mr. Johnson's. I think the interest of the Justice Department here, and in United, was in recognizing that the Justice Department was terribly concerned about the concentration of market power in the entire Washington, D.C., area, Washington Reagan, Dulles, and Baltimore. It would have left a surviving United as the largest carrier in all three of those airports.

United in creating DC Air, and DC Air in eventually partnering with American, was to create some competitive response to that United presence, both in terms of the local Washington market, but also in terms of some traffic flows that can happen through Reagan by building network connecting opportunities between DC Air and American, connecting opportunities that will be competitive with Dulles, competitive with Newark, competitive with a number of the other East Coast connecting points.

Again, I think it was United trying to be responsive to that issue with the Justice Department that led to this deal.

The CHAIRMAN. Mr. Compton, you mentioned that American has made a commitment to absorb responsibility for the TWA retirees' medical and dental insurance benefits. My office has received numerous calls from retired TWA employees regarding their retirement benefits. What is the status of the lifetime term pass, plus-65 medical coverage for retired TWA employees, and the life insurance policy provided by TWA in your negotiations with American Airlines?

Mr. COMPTON. Thank you for that question, Mr. Chairman. That has been a very big concern of ours as well. TWA, because we are a company that has been in business for 75 years, has thousands of retirees, as a matter of fact more retirees than we have active employees. One of the bedrock issues in our discussions with American and discussions that we had previously with others was the importance from our perspective in protecting those retirees.

On the liability side of our balance sheet we have got $509 million, nearly a half a billion dollar liability, for post-retiree medical and dental benefits. Unfortunately, a lot of carriers that we spoke to had no interest in assuming that responsibility, which was very problematic for us. I am happy to say that Mr. Carty and American Airlines has agreed to assume all of that liability. So our retirees' medical and dental insurance is protected.

With reference to the pass issue, there were a lot of things that we had to focus on initially that did not allow time to focus on everything. Mr. Carty and I have spent some time talking about that particular issue and, though we do not have it resolved yet, I am relatively confident—and maybe Don can be more confident than my "relatively confident"—that we will be able to address successfully the retiree pass privileges.

Mr. CARTY. We intend to offer retirees pass privileges, Mr. Senator.

The CHAIRMAN. Thank you.

Mr. Johnson, when you originally entered into a deal with United and you testified before this Committee, you agreed not to sell DC Air for 3 years or you would forfeit the profits from the deal to United. After your deal with American, you negotiated a lifting of that restriction. Why would you lift that restriction in a period of months after committing to the American people and this Committee that you would wait 3 years?

Mr. JOHNSON. Mr. Chairman, I do not think I committed to that. I think that was part of the deal as it was drafted and I had to take it. I never felt that that was an appropriate restriction on my ability to generate value by bringing on an additional partner. That was part of the original deal and to move forward it was something I accepted. But it was never something that I felt was appropriate.

The CHAIRMAN. I am sorry that you did not inform us at the time when you testified before the Committee in favor of this and specifically stated—I think we can review the record—that you were in agreement that you would wait 3 years.

Mr. JOHNSON. No, Mr. Chairman, I have not changed on that point. I have no plans whatsoever. Three, 15, 20 years, I have no plans whatsoever to sell DC Air. But as far as that commitment, that commitment was put in as part of United's requirement because they felt that if I were to sell DC Air and reap a profit they wanted to share in that up side. But it has nothing to do with my personal commitment to continue to own DC Air.

The CHAIRMAN. Well, I tell you, Mr. Johnson, it brings into question the commitment that was made before this Committee of all the details of the agreement that you made with United and was presented to this Committee.

Mr. JOHNSON. Mr. Chairman, if I may comment. The biggest issue for DC Air and United was the question of whether or not DC Air would be independent and free to compete against United. As Mr. Carty just pointed out, DC Air will be able now to compete aggressively against United, against Delta, against the other carriers on the East Coast, with the alliance with American.

On the question of the restriction from United, that to me would have raised even more of a question about our ability to compete by having that proviso in the deal. I would think that the Committee would have wanted that out as opposed to having it in.

The CHAIRMAN. Mr. Johnson, all we wanted was the details of what it was all about, that we were briefed on that and that everybody was in support of it, and in a matter of months it changes. That is clearly your option, but it then understandably leads to increased scrutiny on the part of the Committee, and I thank you for your response.

Mr. JOHNSON. Thank you.

The CHAIRMAN. Mr. Leonard, do you maintain that DC Air would not provide meaningful competition out of Reagan National?

Mr. LEONARD. I believe that DC Air will provide competition and it would obviously bring some advantages with the American frequent flyer program and that sort of thing. But I do not think that anybody in the D.C. area or marketplace is going to see fares any different than what they are seeing today, what US Airways and United charge today. We submitted some documents the last time we were here that showed that it would be virtually impossible to start with United's cost structure, now American's cost structure, and turn that into a low-cost or low-fare airline.

So we believe that the service that is provided today and at the costs and prices provided today will not change at all. We have run a model starting with United's costs and looking at a reduction in costs over time, and our model would indicate that DC Air will be unprofitable in the fourth year of operations.

The CHAIRMAN. Thank you.

My final question. Mr. Levine, when you were working on airline deregulation in the CAB, did you foresee the current structure of the airline industry?

Mr. LEVINE. No. Rather, we assumed that the marketplace would work out solutions that regulators had been unable to foresee. I think we understood that airlines might grow. I do not think we understood the significance of hubs as they emerged.

I ought to say, in my view the industry today is workably competitive. It is a very competitive industry. My concern is that if it moves from an industry in which there are five or six airlines that can compete with each other to two airlines with whom no one can compete, it will cease to be competitive. In both cases Southwest Airlines will exist, but I have tried to explain why Southwest is not enough.

So the short answer to your question, Senator, is we did not expect to foresee exactly what happened. That is part of the point of deregulation, is that a government agency cannot do so. But we expected that the industry would emerge as a competitive industry, and it did prior to this really unprecedented proposal that is on the table.

The CHAIRMAN. Senator Hollings.

I thank the witnesses.

Senator HOLLINGS. Cost structure. Mr. Leonard has just attested to the fact, Mr. Johnson, about the cost structure. Namely—Bob, you are not listening. Watch him. You are making money.

In your testimony, Mr. Johnson, at the previous hearing when I said, I knew you were not an ingrate and if you were going to get the equipment and the slots and the mechanics and the frequent flyer and all the other benefits, as a former member of the US Airways board, and they were selling it to you and it looked like a sweetheart deal, then how were you going to compete? Your answer was that you did not have to subsidize those long-haul expenses, that you would be independent.

I see you shaking your head. Let the record show that the witness shakes his head affirmatively.

Now, having said that, you put American Airlines back into that same situation, that you will have the long-haul expenses of American. I do not see how—I was taking heart that I was going to get, like Mr. Leonard's airline, some small competition that did not have to subsidize the long hauls and, therefore, could reduce the fares. The Vice President of US Airways is present in the audience. He will attest to the fact that I called 2 days ahead of time to get a round-trip ticket from Washington to Charleston, South Carolina, and back. Coach class was $917.

Now, this is not theory or whatever else it is. This has gotten horrendous, Mr. Levine. This has made me a born-again regulator. I wish I had not listened to you folks on deregulation.

The small, medium-sized towns in America are subsidizing the long hauls and the airlines are taking over a monopolistic hub control.

Mr. Johnson, what is your answer now?

Mr. JOHNSON. My answer, Senator, is that DC Air will not have American's high cost structure.

Senator HOLLINGS. Why not? They have got a 49 percent ownership. You are sitting there 50–50 just about. You are not going to refuse them.

Mr. JOHNSON. I am 51–49 and I have control, and I am not going to pay Mr. Carty's high price for the services that he is going to provide. He is going to give me competitive prices that I can either bid out or continue to take from him. I can take the wet leases from him or I can bid them out. I can take his fuel costs or I could bid those out. I can take his ground service costs or I can bid them out.

So I will have lower cost alternatives if I choose to. But my hope is that, obviously, Mr. Carty as an equity player would give me his best price, that I will be able to pass along to our customer.

The other point of fact is we will be a simplified, point to point flying airline. We will not be flying, as I pointed out earlier, we will not be flying the long routes that US Airways currently flies, nor will we be flying the long routes that American flies. So we will be a point to point flyer. A lot of our costs will be reflective of that of a regional carrier, not of one of your big national carriers. So in the leasing of our regional jets we will have a cost structure that is a function of regional jet leases, not of operating with high labor costs and higher employee costs.

The CHAIRMAN. Mr. Carty, would you, American Airlines, go forward with the agreement if the government approval required the breakup of the St. Louis hub?

Mr. CARTY. Would I go forward with the TWA transaction, Senator?

Senator HOLLINGS. Yes.

Mr. CARTY. No. We are very interested in the St. Louis hub.

Senator HOLLINGS. In that hub?

Mr. CARTY. Yes, sir.

Senator HOLLINGS. Well, that points up the dilemma. We are all trying to help the employees of TWA. They are in a struggle. Yet at the same time we are burdened with the responsibility of trying to provide competition, and there is no question that these hubs, 85 percent of the landings and takeoffs, like Charlotte, which I am required to go through by US Air, that there is no competition there. You can just go around the country and see similar examples. I am drawing up a bill now to at least break up the hub control, a bill intended to promote competition.

But your testimony is, then, that you are not going forward with the agreement unless you can extend your monopoly.

Mr. CARTY. Well, we are not looking to extend our monopoly, Senator. We use hubs to participate in the thousands of O and D markets that the GAO referred from the East Coast to the West Coast. We are largely an east-west carrier.

Senator HOLLINGS. In a monopolistic way. Nobody else can go in and cut the fares, the service or anything else. They have tried that down in Texas.

Mr. CARTY. I do not believe we have very many markets on those east-west markets that are monopolies, Senator. Our dilemma today is that the east-west hubs we use—Chicago in the first instance, as you know, is terribly bottlenecked. So our ability to continue to grow our east-west business is bottlenecked by the infrastructure limitations in Chicago that are unlikely to be cured any time in the near term.

In DFW we do have growth potential, but actually in the next 4 or 5 years while we are building a new terminal and a new train system to be able to allow that facility to grow as we know it will, we are limited at DFW as well.

So we are looking for ways to facilitate continued growth in those thousands of highly competitive markets.

Senator HOLLINGS. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Smith.

STATEMENT OF HON. GORDON SMITH, U.S. SENATOR FROM OREGON

Senator SMITH. Thank you, Mr. Chairman.

I fully appreciate as a former businessman myself that sometimes mergers and acquisitions are the best way to retrieve the most public good out of bad business circumstances. But as a current consumer of airline services, I am acutely aware, Mr. Chairman, that big does not equal better. The danger this industry runs, I believe, of re-regulatory pressure from Congress is born out of the fact that to the modern public air passenger service is no longer a luxury, but a necessity.

As Members of Congress, it is increasingly difficult not to hear the chorus of complaints from the traveling public, or to experience them ourselves, I would add.

I am interested, Mr. Carty and Mr. Compton, what would be the effect on prices if this goes forward as opposed to allowing the normal bankruptcy proceedings to go forward? I ask that question simply because I wish St. Louis well. I would like to help. I would like to see this happen. But I am also mindful from what I have heard this morning that you are making a really good deal and you are making everybody whole, and I think that is wonderful, but somebody is going to have to pay for it if your shareholders, as I heard, are going to get the right return on their investment.

So what does that mean to the consumer? That tells me their prices are going way up, not down.

Mr. CARTY. Well, Senator, let me just make the observation that we are obviously not a charitable institution. We obviously have got to make a return on this investment. On the other hand, the reason that we could never make business sense out of a deal with TWA in the past is their liabilities exceeded their assets. In bankruptcy court we are able to go and buy those assets at what we consider to be a fair market value.

If we look at growing our company by 200 airplanes and the cost of building a new hub and the cost of building the passenger loyalty that we need to make that hub work, the cost would far exceed what we are able to buy those assets for in the bankruptcy court. So actually we are making a very good financial deal, one that is better than starting from scratch, and therefore we do not need any unique pricing to make this a successful business venture. It is a successful business venture simply by extending the existing TWA business model and curing some of the defects that TWA has had that Bill Compton referred to. That is, a terribly weak balance sheet and therefore paying way too much for their airplanes due to Carl Icahn.

Senator SMITH. Do you think the economies of scale are such that you can absorb all of these costs, new costs, with other savings so that it will not affect the price of tickets to consumers?

Mr. CARTY. Yes. What I am saying yes, Senator, that the investment in this—we do not need to save costs. The TWA business model that exists today, absent those two or three factors that Bill Compton referred to, is a successful business model. The hub in St. Louis is working now, and by acquiring it at a fair and reasonable price we can make that a satisfactory return.

Senator SMITH. My colleague Senator Wyden, if I know him—and I know him well—he is going to talk about the Passengers Bill of Rights. I have to tell you that regulation to me as a Republican is an abhorrent thing, being a party to that. But I have to tell you that I believe you are playing with fire, because I would personally find it difficult not to listen to all the calls that I get, particularly last summer, about how horrible airline traffic is and waits and discourtesies.

What I am hoping you all will come and educate me about is what part of this is the federal government's fault, what is the FAA doing to complicate your work, and what we need to do to provide a better system. But I would hate to have to vote right now on Senator Wyden's bill, because I would have a tough time voting no. I want a better service for me and the people that we serve. I want to hear from you what the FAA needs to do.

Finally, I represent a state that is sort of off the beaten track and this has not meant good things for Portland, Oregon. I would hope that we would continue to have American Airlines service to St. Louis and TWA as well, but I do not know that. I hope you will answer that.

Mr. CARTY. Let me just make a couple of observations. Obviously, we cannot go through that discussion of the FAA and the ATC challenges today. But we and others in the industry would be delighted to have that dialogue with you.

I want to be very clear—and I have said this to this Committee before—all of the challenges to service in the airline industry do not depend on the federal government. The airlines can do a better job and I have testified to that in front of Senator Wyden under questioning on a number of occasions.

We at American certainly are trying to do a better job. We have tried to restructure our hubs so that they work better. We have tried to do a better job of manning. We have tried to do a better job of a lot of things in the last year, and I can give you a long list of things. We have got another long list this year. We are certainly going to do a better job of deploying data processing devices to help service, help our employees give better service, and so on.

But there is a big piece of this problem that relates to the ATC. I think the new Secretary of Transportation testified to that effect, acknowledged it, and recognized that something needs to change and change dramatically. Under Senator McCain's leadership we had the Mineta Commission several years ago and that is as good a blueprint for fixing some of the air traffic control issues that I think exists.

I know a number of you—and I know certainly Senator Hutchison is very interested in this issue. The airline is interested in this issue. And of course the airline manufacturers have a newfound interest in this. Boeing, as you probably have seen, is trying to come up with a radical proposal to address this issue.

All I would say to you, Senator Smith, at this stage is, with or without a Passenger Bill of Rights, until we fix the air traffic control system those letters that you get, which are a drop in the bucket compared to the letters I get and am not happy about, will not stop.

Senator SMITH. That is all, Mr. Chairman.

The CHAIRMAN. Senator Wyden.

STATEMENT OF HON. RON WYDEN, U.S. SENATOR FROM OREGON

Senator WYDEN. Thank you, Mr. Chairman.

Senator Smith has been so helpful to me, I ought to quit while I am ahead. I thank him for his comments, for his kind words.

Mr. Carty, I come at this this way. First, I think all of us want to be sensitive to Senator Carnahan and Senator Bond and others in the Missouri situation. But the bottom line for me is that when you look at this entire array of mergers that is on the table, it is going to suck up most of the competitive juices that are left in the airline sector. Now, today's level of competition is not doing a whole lot to improve service to the customer.

Now you are proposing more concentration and obviously you are going to be very busy as an airline integrating the new assets you want to acquire from TWA and US Air and figure out how to operate the shuttle.

My first question to you is, given all that, what commitments will you make this morning specifically to improve life for the passengers?

Mr. CARTY. Well, Senator Wyden, as you know, I think it is fair to say that American has been on the front end of that in the last year. We have provided our customers with a lot more space in the cabin. We have restructured hubs. We have had a series of programs that have been designed to do that.

But as I testified to Senator Smith, Senator Wyden, I honestly have to agree with the Secretary when he testified that we are not going to fix this problem as quickly as all of you and I can assure you that all of my meeting team and I would like. This is a terrible challenge.

You will see around the room a number of pilots from TWA. If you want a real story of the horrors of flying in this country in the context of congestion and difficulties, they are probably far better equipped than I to testify to it. But I wish I could assure you this problem is going to get fixed. I would be disingenuous if I testified to that.

Senator WYDEN. What I disagree with in your argument is you are saying again that you and the industry really will not take significant steps to help passengers until you get more runways and a better air traffic control system. We are with you on more runways and air traffic control. Clearly it needs to be improved, and FAA permitting as well. But the idea that you are not going to make any commitments to passengers now, when there are steps that you can take for those people that sit out on the runways for hours on end with a little bag of pretzels and a glass of water, is just unacceptable to me.

Once again this morning, you have said: Well, it is just up to getting more runways. I think that is unfortunate.

Mr. CARTY. I am sorry if you heard that, Senator. That is not what I said.

Senator WYDEN. You send to us in writing what specific commitments you are willing to make to improve life for the passengers as a result of this array of deals that you are involved in; I am happy to take a look at it.

Mr. CARTY. I will be glad to do that. It will have nothing to do with the array of deals. I will do that regardless.

Senator WYDEN. Why are airlines different than other sectors? I mean, what we have been told—and I have sat through all the hearings on antitrust here—is that one big merger follows another, and if this array of deals goes forward two airlines are going to dominate 51 percent, more than 50 percent, of the airline business. Are we not as sure as the night follows the day going to be back here in 6 months for the last one?

Mr. CARTY. I think—what makes the airlines different, was the question. I do not know that anything does uniquely, Senator. Of course, we have seen mergers and acquisitions in a lot of industries, far bigger ones, far more concentration than you have yet seen in the airline business. We buy a lot of fuel and I have watched 20 and 30 and $40 billion companies merge with really almost zero in the way of remedies proposed by the government.

I am not going to sit here and defend United's package of remedies. But I will say they have already indicated a willingness to divest themselves of some 20 percent of what their are acquiring. Now again, that may or may not satisfy this Committee, these remedies.

But what drives us to do this? Because network is one of the competitive vehicles. It is not the only one, but it is an important one.

Senator WYDEN. Supposing that we separate out these deals so that we can be responsive to Senator Carnahan and the Missourians and we in effect say American takes over TWA, but the United-US Air merger does not happen and the American deal with United and DC Air does not happen. Would not that kind of scenario result in less concentration of the market, address Senator

Carnahan's concern, and avoid harming competition to the consumer?

Mr. CARTY. Well, it would certainly address the TWA concern. I might add, I neglected because Senator Smith left to make a commitment to Portland-St. Louis, but all I can tell you for sure, unless that hub survives there will not be service between St. Louis and Portland.

But to your point, again I think that decision needs to be made carefully.

Senator WYDEN. You are open to that? So I can be responsive to Senator Carnahan, who has made such a good case for her constituents? You are open to separating out the deals along the lines I described?

Mr. CARTY. Senator, I will simply say the two deals are unrelated. They happened to get announced the same day, but they are not interdependent one on another.

Senator WYDEN. Mr. Chairman, I would only say as we take a look at this that we just can no longer look at these deals in abstraction. I mean, what you have heard in the antitrust hearings that we have held before the Committee through the last Congress is, just as sure as the night follows the day, one is going to follow another. The fact that Mr. Carty is willing to look at separating out these deals is something I hope this Committee will look at on a bipartisan basis.

I thank you.

The CHAIRMAN. Thank you.

Senator Allen.

STATEMENT OF HON. GEORGE ALLEN, U.S. SENATOR FROM VIRGINIA

Senator ALLEN. Thank you, Mr. Chairman. I am sorry I was gone. I had to preside on the Senate floor and that precluded me from hearing all the testimony. My duty as presiding officer precluded me from hearing all the testimony, and also it was not proper to be inattentive in reading all the statements that were made here while presiding on the Senate floor.

The CHAIRMAN. As I mentioned, it is our practice to go according to early bird, the ones who are here first, and if you are required to go preside then we preserve your priority. I hope Senator Fitzgerald appreciated that as well.

Senator ALLEN. It surprised me that you called on me. I know I was here early and had to leave.

I would only make a few comments in this regard and I would like to address some questions or comments to the panelists here. The issues of consolidation in the airline business is a concern to all of us. The concern for all Americans, of course, is competition and thereby service. Then in our individual states we care about service to the airports and the citizens of our state, as well as the companies, such as US Air, that have a very strong presence in our state. TWA has a reservation center in the City of Norfolk. DC Air has put a maintenance facility in Roanoke, which is helpful.

But overall, and I think it is very timely for this Committee to have a hearing on this to help us understand and thereby our constituents understand what is going on here. But the issue of market consolidation in my perspective, in my view, is not just unique to the airline industry. Especially in the area of transportation, it seems to be happening everywhere, from the steamship lines, with someone buying Sea-Land from CSX and the alliances of steamship lines, whether it is in Europe or in the Pacific, Far East Asia area.

The same thing is happening in the railroads as well, trying to get efficiencies of scale, getting greater economics and thereby helping make their employees even more productive.

Now, this consolidation is one that—more people fly than go on a container ship, so all of us understand this on a personal level. I think that we need to make sure that the aviation market is competitive, safe, and efficient. I think that safety and efficiency are generally the province of the Federal Aviation Administration and this Committee clearly has a lot of work ahead in my view as far as fixing the antiquated and outdated air traffic control system.

But there are acts that have been passed by the federal government, by the Congress, on the issue of compensation, which are known of course as the Sherman and Clayton Acts, and they do have very clear directions that are given, guidelines, which the Department of Justice must analyze in any potential merger that could impact an industry.

Obviously, the US Air-United merger is getting attention. The focus here, though, is mostly obviously with the participants on TWA's precarious situation, financially precarious situation, and American Airlines' acquisition thereof, and then how the whole thing comes out with DC Air and the different aspects of it.

As I see the TWA situation, if nothing happens with TWA they are clearly going to go bankrupt. I would not call the people who buy up the different assets and routes and slots and so fort buzzards. They are just folks that are like any other bankruptcy sale, they are buying chairs, desks, assets, and so forth. That is the way bankruptcy—that is the way some types of businesses turn out.

To me this seems to be a very logical approach to try to save those jobs, save those routes. I would want to make sure that the jobs, with this convergence, that the jobs that are already in existence to the extent possible can be kept. I do not know what kind of assurances or promises can be made, but it seems to me that the Department of Justice is getting certain promises in the midst of the US Air-United situation which are in addition to the original merger proposal.

I would like to ask Mr. Johnson, DC Air, since you will be operating out of Reagan National Airport in Northern Virginia, how do you see your situation benefiting the people along the East Coast, which is where you are mostly going to be servicing? How do you see the eastern seaboard, Virginia, the rest of the East Coast benefiting from your new service?

Mr. JOHNSON. Thank you, Senator. I think the key component of DC Air and the key commitment we made at Reagan National Airport is to take the slots that were formerly flown by US Airways and continue the commitment to fly to those 44 communities that have been served, in some cases for over 40 years. So all of those communities will continue to have direct access to Reagan National Airport, which is most important to many of these small communities.

It is my belief, and I think it is the fact, that if those slots were parceled out the individual carriers, many of the smaller communities, like some of those in Virginia that are not concentrated communities as far as traffic, will lose service if you take those slots at Reagan National Airport and sell them off piecemeal or hand them out piecemeal.

What we have made a commitment to do is that we will fly, as long as it is economically viable—not economically viable against flying to another community or against flying to a more attractive market, but as long as it is economically viable within that community—we will pledge, and we will put it in a consent degree, to continue to fly to these 44 communities, and we will also fly in upgraded aircraft. We will try to move as quickly as possible from turboprops to all all-jet regional jet carrier.

Senator ALLEN. The Bombardiers?

Mr. JOHNSON. It will be that or some other type of aircraft that will give us the number of seats that are necessary for the route.

In addition, with the American Airlines alliance, the marketing alliance, our passengers will have access to the full frequent flyer program of American Airlines for the entire global system. So we are offering a very attractive package. There will be lower costs because we will have wage and pay scales that operate on a regional basis rather than on US Airways' high national basis.

So we think, Senator, that the key for Reagan National Airport, the key for the Washington region, is for those slots to remain intact under the control of a competitive carrier that will serve those small communities.

Senator ALLEN. Is your commitment to the Department of Justice or in this merger—when you say you are making a commitment, and for that matter the folks, Mr. Carty with American, can answer this as well, the promises to serve these markets, how long? What is the duration of this promise?

Mr. JOHNSON. My promise, Senator, as long as I own the airline.

Senator ALLEN. Well, is it binding in the event that somebody thinks it is a good airline? What if you sold the airline?

Mr. JOHNSON. Well again——

Senator ALLEN. Or there is another merger?

Mr. JOHNSON. As I said, I am prepared to go on the record, I am prepared to make it part of a term of the deal, that as long as I am the owner of the airline the cities, like Norfolk, Richmond, and Roanoke and other cities like that throughout—Huntsville, Birmingham; I can name them all; Charlotte, Greensboro, all these small communities, Nashville, Knoxville—will continue to receive direct service from Reagan National to these communities.

Senator ALLEN. And thereby get them to, for example, St. Louis and to the West Coast?

Mr. JOHNSON. Get them throughout the entire American system. We will not only have frequent flyer, we hope that we can negotiate a code-share with American, so that when you look at—when the travel agent looks into a DC Air flight, they will see the vast array of connectivity that American will bring.

I think one of the things that people need to recognize in the DC Air-American alliance, we bring a lot of connectivity to Reagan National Airport now with American. So Reagan becomes for us somewhat of a hub connecting to American's vast network, and that is one of the most attractive things about the DC Air commitment.

Senator ALLEN. I would say, Mr. Chairman—I guess my time has expired.

The CHAIRMAN. Thank you.

Senator Dorgan.

Senator ALLEN. May I just make one—one thing that would be very helpful I think to every Senator is, as you get into these things, as US Air, TWA and so forth serve these areas, if you can get a list of, here is the number of flights currently and here will be the number of flights under this new situation, I think, in airports amongst all our states and places served, that will help us understand that competition will continue.

Thank you, Mr. Chairman. I am sorry.

The CHAIRMAN. Senator Dorgan.

STATEMENT OF HON. BYRON L. DORGAN, U.S. SENATOR FROM NORTH DAKOTA

Senator DORGAN. Mr. Chairman, thank you very much.

I have ridden on all three airlines that are represented here today by their chief executive officers. All good companies, and we appreciate your testimony.

But I do not even know where to start in this discussion. I have been sitting here trying to figure out how you begin to ask question in these areas. I would make a wager to any of you at the table that we could leave here after this hearing and get on the telephone and I can find an airline fare to Paris that is cheaper than an airline fare to Charlotte. It is going to be less expensive to fly to Paris than Bismarck, North Dakota.

The reason I mention that—if anybody wants to take the wager, I did that last week, so I would know I would win. But Mr. Levine, when you say there is aggressive competition in this country, you are wrong. What we have is unregulated monopolies in regional hubs. The big airlines have retreated to regional hubs, dominate the hub, and we have unregulated monopolies.

I guess we have a lot of interests here. We have interests at the table representing the company. We have interests of the employees. We have interests of financiers and others who are not here. The interest I think this Committee represents is the interest of the American people to try to evaluate what needs to happen here to maintain a good transportation system, a network of airline carriers where you have some reasonable competition.

With respect to TWA, in the mid-1980's I was serving in the House. I was highly critical of what happened when TWA became a pawn in the leveraged buyouts. It became a football with financiers treating it as something they could make money off of, and they succeeded, moving it through two bankruptcies, for a lot of reasons. I felt it was a shame at the time that that happened. Of course, a decade and a half later we are here at the table and you are pleading that your company can be purchased by American and the employees are not so severely disadvantaged and you have an ongoing enterprise.

Regrettably, a decade and a half later you are still cinched in that saddle that was put on you back in the mid-eighties.

I do not know where we go here. I guess I would just say this. We need more competition in the airline industry, not more concentration. I am not under any circumstance willing to be a Member of Congress and be silent while we move toward three major airline carriers dividing up our country. It is not in this country's interest to do so.

Mr. Carty, you and I have had discussions and I admire your work at American and I think American is a great company. Tell me, if you will. You represent your company and represent it well. But from the vantage point of people who represent the long-term interests of the American consumer, how on earth can more concentration be in the interest of the regulation consumer?

Mr. CARTY. Well, if you are speaking, Senator, to the TWA transaction, TWA is going away one way or another. The question is is there going to be a hub in St. Louis or not, and if there is not that cannot be in the interest of the consumer that wants to get from Portland, Oregon, to St. Louis, because he will now have to go through Chicago, Minneapolis, or Denver.

I would simply say to you, I think that is a very black and white issue. If that hub fails to survive under anybody's ownership, that cannot be in the interest of the U.S. consumer.

Senator DORGAN. I understand your point. But the other gorilla not at the table is also part of this hearing, and that is the United Airlines-US Air issue. We are not going to be able to deal with these things in isolation. Frankly, we are headed very quickly, I think, to a circumstance where three major carriers, because the others are going to have to do something defensively, three major carriers will be involved in commanding most of the traffic in this country.

I just fail to see how that increased concentration is in any way other than detrimental to the American consumer. Now, I was told—I grew up where there were raccoons and raccoons when they eat, they get their food and wash it in streams and lakes and they wash it meticulously. But even when there is no water around, they go through the exact identical motions to make it appear as if they are washing food despite the fact there is no water, so they pantomime.

I was thinking about that this morning. We kind of are in a circumstance where I am seeing some pantomime competition develop here. We do not have competition into Bismarck or Charlotte, not real competition. What we see with more concentration is we are going to have pantomime competition, but it is not going to be real for the American consumer.

The only way the system works, I would say to all of you—this is therapeutic for me to be able to say this, so I am sorry I am not asking you questions. This free market system works only when you have free and open competition, easy entry and exit. It seems to me concentration clogs the arteries, it is the cholesterol that clogs the arteries of the free market system, and we are relentless in this drive toward more concentration.

Mr. Levine, I know you want to answer me, but I would say I just think you are dead wrong when you say there is aggressive competition. What we have is monopolies in regional hubs, dominated by one carrier, in almost every circumstance in this country.

Mr. LEVINE. Mr. Chairman, do the rules of the Committee allow one to answer when addressed?

The CHAIRMAN. Yes.

Senator DORGAN. I would invite you to answer me, of course.

Mr. LEVINE. I think it is important to understand how hubs work. There are very highly differentiated price structures in those hubs. The average prices in the hubs and in the system are quite low and they are lower than they were under regulation. But there is a lot of price differentiation and some, relatively few, passengers pay very high fares for the convenience of having a hub.

People have been talking about Charlotte, a hub I have had no responsibility for and so no one can say that I am defending as my handiwork or anything like that. Charlotte is a hub that provides nonstop service to many, many cities that would get no nonstop service to Charlotte if there were not that highly differentiated price structure were not in place. I should point out that despite fares which seem high, Charlotte is a hub that loses money.

The fact is that in order to provide frequent nonstop service at the hub it is necessary to charge somebody for that convenience. I understand that it is infuriating, really infuriating——

The CHAIRMAN. That understates it.

Mr. LEVINE.—to pay four times or five times as much as the guy sitting on the plane next to you. Nobody likes that and I am not suggesting that we will learn to like it.

You know, let me talk about one of the great blues singers of all time, Albert King, who used to sing a song that went: "Everybody wants to go to heaven, but nobody wants to die."

The story about hubs is that everybody wants nonstop service to a lot of places, but nobody likes to pay for it.

Senator DORGAN. But the story about blues is that everybody in small markets sings them after deregulation, because we have less service at higher prices, and that is the fact.

I do not have the slightest interest in averages. You know the old story about one leg in ice water and the other in boiling water on average is pretty comfortable. I do not have the slightest interest in averages. On average, we pay the highest prices in the world in these rural markets. Olympia Snowe and I have talked about this and others have. In our markets, we no longer have any serious competition. That is why Fritz Hollings gets so excited about this, and others of us do as well.

The question today is whether we have a big old pie that people are slicing up for their own interests. I am hoping we can find—I flew Braniff, Western, Eastern, and Pan Am. I flew on all those carriers, and they are gone and we are talking now about, well, how do you slice up what is left? But the question for us is what does all this mean to the American consumer? What kind of system do we have in 10 years and what does it mean to the American consumer? That is what I am interested in. That is the interest at the table that needs to be discussed.

Mr. LEVINE. I just want to be clear. As you know, I am here objecting to the transactions that are the particular focus of today's hearing.

Senator DORGAN. I understand that, Mr. Levine, I think you have done a lot of good work. I do not think deregulation was your best work, but I think you have done a lot of good work and a lot of good writing. I would just say, when you said, gee, there is a lot of competition, I just sat up and thought, why, I do not want to let that sit out there, because in many areas of the country there is really no competition.

But thanks for your good work.

Mr. CARTY. Senator Dorgan, if I could respond just a little bit.

The CHAIRMAN. Mr. Leonard and then Mr. Carty, and then anybody else who would like to make a brief response, if that would be agreeable. Mr. Leonard.

Mr. LEONARD. The only comment I would make is that airlines like AirTran, jetBlue, and Frontier that are successful network airlines, but smaller, and are perfectly willing to provide the competition and lower the fares in the markets, as we do in Atlanta. We run up against one of the strongest airlines in the world every day and we do very well with them. If we had access to other airports, facilities, gates, and other physical facilities, we are perfectly willing to go into these other markets and provide that service. But we are constrained from that because you cannot get gates, you cannot get slots, you cannot get some of the other facilities that you need.

I think this is an opportunity to change that. I think this is a real opportunity to change that and require carveouts as part of these acquisitions that are going forward.

Mr. CARTY. Senator Dorgan, just a couple of observations. The market is a mysterious place and there are two places—there are two positions in the market, the seller and the buyer. Joe Leonard mentioned the average published fare between Chicago and DCA. The biggest single buyer in that market is the federal government. The federal government buys that product from both United and American at less than $100, because they have got buying power, and that buying power creates enormous competition between American and United for that big block of business.

So part of the vagaries in the market are the strength of the buyers as well as the strength of the seller.

To your other question, though, and I think this is a very interesting one and one I am interested in, and that is small communities. I genuinely believe we mix up business with needed economic development issues. I think the EAS program in this country is today inadequate to accomplish what many of you would like to accomplish for your smaller communities. For one, I would be supportive of a complete relook at the EAS program, because I do not think it encourages carriers to serve those communities.

The carriers that serve those communities are not necessarily American. They are not even AirTran and the jetBlues. They are, as you know, in many instances smaller carriers that operate smaller airplanes, and they have a very tough time making a dime. I would be glad to participate in that discussion.

The CHAIRMAN. Do you have a brief comment?

Mr. COMPTON. Yes, I do, Mr. Chairman. Just briefly, I think, coming back to the TWA issue once again and the effect on competition, the fact of the matter is, unfortunately—and you named all of those other airlines. My father was a Braniff employee, so I have experienced it, he has experienced it, and it is a sad situation when a company just goes away, for not only the employees and the retirees, but the communities we serve and our customers.

What happened with those other airlines is they went away. The circumstance that we have got here is that either TWA will go away and the 187 aircraft that we fly will go to the ground for some period of time—some Pan Am and Eastern airplanes are still in the desert and have not been flown since those airlines shut down—and you will be taking capacity out of the system and diminishing competition and diminishing choices for the consumer.

I look at, for example, TWA flies six times a day between Cedar Rapids and St. Louis with full-sized jet aircraft. Without the St. Louis hub, I would argue that places like Cedar Rapids—and I could name 25 cities like that—would be severely disadvantaged. So unfortunately, our circumstance is one in which TWA will go away, will take capacity out of the system, will disadvantage employees and retirees, will disadvantage the consumer, and will disadvantage communities.

So from our parochial perspective, we think that the deal with American Airlines is a win for all of the stakeholders.

The CHAIRMAN. Mr. Johnson.

Mr. JOHNSON. Senator, I would be remiss if I did not remind the Committee that the greatest blues singer was a guy named Robert Johnson. The point is that this Robert Johnson is a new entrant, and I think people tend to forget that. There is new competition being created out of the merger of United and US Airways. It is called DC Air, a new entrant, a minority-owned entrant and one that will be competitive on the East Coast against the other carriers in and out of Reagan National Airport.

So I do not want to lose sight of the fact that there is no new competition, Senator, coming on the scene.

The CHAIRMAN. Ms. Hecker, do you have anything?

[No response.]

The CHAIRMAN. I thank you. I would like to announce, in my 4 years as Chairman of this Committee we have set a record for metaphors—very illuminating.

[Laughter.]

The CHAIRMAN. Senator Fitzgerald.

STATEMENT OF HON. PETER G. FITZGERALD, U.S. SENATOR FROM ILLINOIS

Senator FITZGERALD. Thank you, Mr. Chairman. I really want to thank the panel. I think this has been an excellent hearing.

I have a question for Mr. Johnson before I go on and ask some more direct questions of Mr. Carty. But just out of curiosity, how much money did you put in to capitalize DC Air, and has that money been put in already? It is not up and operating.

Mr. JOHNSON. Senator, to date in the process of going through this transaction I have invested a little over a million dollars in what I call startup expenses, and I have acquired a line of credit in excess of $70 million.

Senator FITZGERALD. So you have invested about $71 million?

Mr. JOHNSON. $71 million is available to me that I have to invest, and it will probably go up higher than that. It will probably end up being about $100 million all in.

Senator FITZGERALD. But now, you are selling 49 percent of your interest in DC Air, which you now own 100 percent of——

Mr. JOHNSON. That is correct.

Senator FITZGERALD.—to United, and how much are——

Mr. JOHNSON. To American, Senator.

Senator FITZGERALD. To American, I am sorry.

How much is American paying you for that 49 percent?

Mr. JOHNSON. It would be approximately $67 million.

Senator FITZGERALD. So on a million dollars cash, $70 million borrowed, to capitalize 100 percent of the company, you are selling 49 percent of it to American for, did you say $70 million?

Mr. JOHNSON. Approximately, $67 million.

Senator FITZGERALD. That is a real good return, and you have not borrowed yet.

That is maybe why he wanted to enter the airline business, Mr. Carty. You wondered about that.

Mr. CARTY. I think there is a little confusion, Senator Fitzgerald. We are both putting in substantial amounts of money. He is not taking a million dollars and selling half of it to us.

Senator FITZGERALD. He owns 100 percent of the stock right now, correct?

Mr. CARTY. We are putting our money into the company.

Senator FITZGERALD. Okay. But he is going to——

Mr. JOHNSON. That money is not coming back into my pocket. It is going into the company.

Senator FITZGERALD. Okay, but it is enhancing your other 51 percent. What is the value of your 51 percent right now versus what it will be after they put in——

Mr. CARTY. We are putting in the money pari passu, Senator.

Senator FITZGERALD. He is putting in——

Mr. CARTY. He is putting in equivalent with us.

Senator FITZGERALD. Right, but he was going to have to put in that. He was going to borrow that $70 million anyway.

Mr. JOHNSON. That is right, Senator.

Mr. CARTY. Each percent that he buys is costing him as much as each percent we are buying. So he is actually putting in more than we are.

Senator FITZGERALD. And your book value of your shares will go up after they put in their cash.

Mr. CARTY. The total book value of the company will go up, but his share of the book value will stay the same.

Mr. JOHNSON. Will stay the same.

Senator FITZGERALD. All right.

Mr. JOHNSON. So it is not as good as it sounds, Senator. This is not a sweetheart deal, Senator.

Senator FITZGERALD. Back onto focusing on the Midwest, Mr. Carty, you have a hub at O'Hare. You will acquire TWA's hub at Lambert Field. What effect will your owning another hub in the Midwest nearby in St. Louis have on your hub operations in Chicago?

Mr. CARTY. We do not anticipate any major changes in our hub in Chicago, Mr. Fitzgerald. As you know, because of the limitations on O'Hare and the fact that neither we nor United can really get much more capacity into O'Hare absent another runway, we have been shifting the traffic we carry at Chicago gradually to more and more and more local traffic and less and less connecting traffic, simply because we cannot add capacity as the market grows.

So St. Louis gives us a complementary outlet to begin to participate in the growth of those east-west markets.

Senator FITZGERALD. It would make it easier for you to shift some traffic out of O'Hare, which has been at capacity since 1969 now, to St. Louis, right?

Mr. CARTY. But O'Hare is a very rewarding place for us to be, and we are going to use all the capacity at O'Hare we can lay our hands on.

Senator FITZGERALD. That you can get.

Now, you have, you and United, which have 83 percent of the market at Chicago O'Hare, have long opposed the construction of a third airport. I know we have had friendly conversations about this before. I fear that the reason United and American oppose a third airport in Chicago is because you have 83 percent of the market and you do not want new entrants to come in and have all this access with no barriers to getting in and operating at a third airport in Chicago.

Are you going to be even more opposed now to a third airport now that you have got two hubs to protect in the Midwest? Will you ever—in return for doing this deal with TWA, would you consider dampening for 1 minute your steadfast opposition to the third airport in Chicago?

Mr. CARTY. Let me, Senator, clarify American's current position on a third airport. If people want to build a third airport, we are perfectly happy to have them build a third airport. We obviously do not want to pay for it because we do not want that third airport for our use. We are more interested in another runway to complement our O'Hare activity.

But if the city, the state, the country, decides a third airport is a good thing to have at Chicago, we are perfectly happy to have it.

Senator FITZGERALD. I sense some softening there. I mean, that sounds like a little bit——

Mr. CARTY. You are so convincing. I hope I can be as convincing on another runway at O'Hare.

Senator FITZGERALD. Well, you want another runway at O'Hare because you and United would be able to capture that added capacity if it is at O'Hare. You are not so sure if it goes to a third airport which you do not control. You would not necessarily wind up controlling the new capacity if it were at a third airport.

Mr. CARTY. It is more, Senator, this phenomenon I referred to a moment ago. We are losing market share at American, at United, and Chicago O'Hare. Chicago is diminishing in its importance as a hub because we can carry less and less connecting traffic at Chicago. The reason Chicago is becoming less and less airport relative to the Atlanta's and the DFW's and so on is because we do not have the capacity we have at those other airports.

Senator FITZGERALD. That was a good—you skirted it a little bit, but that is okay.

I would be interested to see what your plans would be with respect to the commuter air travel from downstate Illinois to Lambert Field in St. Louis. Right now TWA Express does those commuter flights from places like Quincy, Springfield, into St. Louis. As part of the bankruptcy reorganization, will you reaffirm the contract with TWA Express? Will you get rid of TWA Express, bring in American Eagle to serve those places, or will you not commit to any continued service?

Mr. CARTY. We are now, Senator, in an active dialogue with the TWA Express carriers. There is more than one. There are actually, I think, three, and we are in contact with all of them and have an active dialogue going to them. What I will say to you is that we want that feed at Lambert Field. It only makes——

Senator FITZGERALD. But you own American Eagle as a subsidiary of yours and I would think it would be easier for you to put American Eagle in those communities rather than to reaffirm the contracts that TWA Express——

Mr. CARTY. Actually, Senator, because of Eagle's capacity planning they do not have the resources to provide the commuter feed at Lambert Field over the next 2 or 3 years. So we intend to work with those carriers to make that happen. I would say this to you: if it makes economic sense for them to feed TWA, I would hope, with our expanded network at Lambert field, it would make even more sense for them tomorrow.

Senator FITZGERALD. So you do not anticipate the diminution of service from those places in central and southern Illinois into Lambert Field as a result of your acquisition of TWA?

Mr. CARTY. I certainly do not. Again, these are decisions that each of those carriers make on their own merits. But given that they have not at this stage reduced those services feeding TWA, I would think the economic opportunity for them would be even larger as we build a stronger network in St. Louis.

Senator FITZGERALD. Finally, on the pension liabilities. Mr. Compton, you said you have $500 million, a half billion, in unfunded pension obligations. Is American Airlines going to assume 100 percent of that unfunded pension obligation?

Mr. COMPTON. It is actually post-retiree medical and dental liability. The pension plans were taken over by, the defined benefit plans, were taken over by Carl Icahn in the first bankruptcy, and that plan had been terminated by Carl Icahn and is now administered by the PBGC, the Pension Benefit Guaranty Corporation.

Senator FITZGERALD. So the taxpayers already had to bail that out.

Mr. COMPTON. To some extent. TWA coming out of the bankruptcy was required to fund—even though Icahn took over the administration of the plan, TWA had to fund $300 million. We did that. We accomplished that by 1998. Now, what we did when the pension plans were frozen and taken over by Icahn in 1993, we converted our employees to defined contribution plans. So it is a monthly contribution into their pension plans, and those are portable, 401k's for example. So the employee can take that defined contribution plan at TWA, it is portable, roll it over to an IRA or take it over to an equivalent plan at American Airlines.

So the employee will not be disadvantaged in any shape, manner or form with reference to pension, but will be advantaged with reference to medical and dental benefits which they would not have gotten if TWA was liquidated.

Senator FITZGERALD. As part of the bankruptcy, none of these pension or—I should not say pension—health or retiree benefits will be sought to be wiped out in the bankruptcy court?

Mr. CARTY. No. We have affirmed our responsibility for those.

Senator FITZGERALD. So you will take them all over.

Mr. CARTY. One of the liabilities we are taking as part of the process and have contractually committed to take is the post-retirement health.

Senator FITZGERALD. Now, I gather from reading things about the bankruptcy court case that——

The CHAIRMAN. Senator Fitzgerald.

Senator FITZGERALD. All right, all right.

The CHAIRMAN. Your time has expired.

Senator FITZGERALD. Thank you all very much.

The CHAIRMAN. Thank you very much.

Senator Boxer.

STATEMENT OF HON. BARBARA BOXER, U.S. SENATOR FROM CALIFORNIA

Senator BOXER. Mr. Chairman, thank you for putting together this excellent panel.

I wanted to say, you have all been I think very forthcoming. I wanted to compliment Ms. Hecker because—you know, I rely a lot on your work and the work of your agency. I think you have done a good job of explaining what the long-range situation is.

With all the talk about blues and jazz, I hope everyone has watched Ken Burns' documentary. If you have not, watch the reruns.

I look at the two issues before us as very distinct: the TWA bankruptcy, which I see demands our immediate attention. I could see a lot of employees of TWA here and I am sure they are hanging on our every word, and this is not just some intellectual discussion we are having. As I know and Senator Carnahan and Senator Bond know, it is very real for a lot of people, a lot of families.

Second, American's role in the United Airlines-US Air merger. So I look at those very differently. My immediate concern is the TWA issue. My long-term concern mirrors that of a lot of comments here. I thought Mr. Levine laid those out, as well as Ms. Hecker. We want to make sure that our people, who are becoming so dependent on air travel, are going to be served in the long run.

I would say to the airline people, your big problem is that we are all million mile flyers, so we know firsthand. Sometimes we have businesses come before us and we do not really have that much expertise, but we do when it comes to air travel.

I was glad that Mr. Carty said he looks at these two issues separately. I was wondering—you said you put them out on the same day in a press release. Why did you do that?

Mr. CARTY. I mentioned in my remarks, Senator Boxer, that it was almost coincidence. I had the great good fortune to have the financial analyst community conclude that I was brilliant, but it really was just pure coincidence. The two deals happened to come together. We had been negotiating with United for a very long time, and on the TWA side suddenly it became apparent to us, which it had not before, that TWA was going to have to file for bankruptcy. That created an opportunity and we went into a very intense period of negotiation and discussion with TWA that culminated in the agreement.

Senator BOXER. Mr. Levine, it has been stated here by Mr. Compton, I think in a pretty straightforward way, that he is very concerned about TWA employees and retirees and creditors and consumers and communities served by the carriers, and he feels that if this does not happen and if this thing just goes off into a lot of different pieces it could be terrible for all those groups. I wonder if you agree with that.

Mr. LEVINE. I think that if TWA does not get acquired by American it will be very difficult for someone else to attempt to run a hub at St. Louis. I think it is going to be so difficult for American that I have expressed some question as to whether its shareholders will in the end benefit from this transaction, but that is not your problem. That is Mr. Carty's and his shareholders' problem. I think it is very unlikely that anyone would attempt to run a hub at St. Louis if the result of the bankruptcy is a liquidation of TWA.

Senator BOXER. I wonder, Ms. Hecker, if you would agree with that?

Ms. HECKER. I think one of the interesting things about TWA is how many airlines have looked at it over the past few years and attempted to assess whether it was a profitable acquisition. I think the records show that no one saw that both its encumbered assets and the fact that——

Senator BOXER. I am not asking you that. I am just asking you, do you agree with Mr. Compton that, if your concern is TWA employees, retiree, creditors, consumers, and communities served by both carriers—do you agree with what Mr. Compton said, that if they do not go this way then those, all those interests, would be not as well served?

Ms. HECKER. I agree there is a substantial risk of that.

Senator BOXER. Well, let me say that to me that is of paramount importance, both Ms. Hecker and Mr. Levine saying this, because I do think in this time where we are seeing such massive layoffs, Mr. Chairman, around the country for various reasons, an economy slowing and so on, I think the last thing we need are pensioneers who suddenly do not have their health care and employees who suddenly do not have anywhere to go.

Let me ask you, Mr. Carty, in my remaining time. How many people, more people, will you be taking from TWA? Or maybe Mr. Compton knows that. If in fact you intend, you say, to employ everyone, how many people is that?

Mr. CARTY. It is about 20,000. Bill?

Mr. COMPTON. Right.

Senator BOXER. 20,000 people would continue in employment. Would you bring them in at their same level of pay or integrate them into American Airlines' pay? Have you thought that through yet?

Mr. CARTY. By definition, Senator, they will become part of the American Airlines system and therefore the contracts that the unionized people at TWA operate under will be the American Airlines contracts. Quite frankly, for most people it means a pay increase. The question of how they are integrated and so on really is largely up to the unions to work through.

Senator BOXER. But it is in fact your intention to keep them all on board?

Mr. CARTY. Yes.

Senator BOXER. And to make them part of the parent company, American Airlines.

Mr. Compton, did you get any other offers as good as this one?

Mr. COMPTON. Unfortunately, I got no other offers.

Senator BOXER. What is the time frame that we are looking at here, Mr. Compton, for this to be as smooth as it could be? What do you see as a drop-dead date for this thing to be completed?

Mr. COMPTON. We have got a couple of important dates coming up. We had an important date last weekend in the bankruptcy court, where Judge Robinson allowed the bidding process to begin so we can bring some order to this process. We now are looking for in the first half of March, towards the middle of March, the final sale hearing. Then there will be a period of time to move forward to the closing, but no more than a matter of months.

So it is very important from TWA's perspective to try to resolve this as quickly as we possibly can to the benefit of all of our constituents.

Senator BOXER. Are your people still getting paid at this time?

Mr. COMPTON. Absolutely.

Senator BOXER. And they will, if this all goes smoothly under this bankruptcy filing, until they get taken over?

Mr. COMPTON. Absolutely.

Senator BOXER. Last question. How many cities does TWA currently serve?

Mr. COMPTON. Approximately a hundred.

Senator BOXER. They will continue to be served, Mr. Carty? That is your plan?

Mr. CARTY. That is certainly our plan, Ms. Boxer.

Senator BOXER. Thank you very much, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Boxer.

Senator Hutchison.

STATEMENT OF HON. KAY BAILEY HUTCHISON, U.S. SENATOR FROM TEXAS

Senator HUTCHISON. Thank you, Mr. Chairman.

I have listened to all the questions and I think most areas have been covered. I want to say, as the new Chairman of the Aviation Subcommittee, I plan to work closely with the Chairman on the air traffic control system. We also must remove barriers to infrastructure improvements, because that clearly is a factor in the problems that airline passengers are having dealing with delays and passenger service.

However, I want to also say that I think there are still more things that the airline can do in the area of scheduling that would also bear on the terrible delays and frustrations of the traveling public, and I will expect the airline to do their part if we do what we can do to smooth the infrastructure both in the air traffic control system and the runways and the terminal improvements that are needed.

I find it interesting in all of the hearings that I have attended on these subjects that very often I hear people talk about the free market when it comes to deregulation, but they do not talk about the free market so much when it comes to mergers. I think we have got to tread very carefully in this area, and I think the example that we have made with American and TWA is the wrong one, even if you are a person who is concerned about too many mergers.

I am concerned about the lack of competition. I had great concerns about deregulation. I think, with all due respect, deregulation has not worked. I think the hub system has caused the increase in prices in airline tickets, and I think that perhaps some other partial deregulation might have been a better answer than what was done by Congress.

But we are where we are. Deregulation, the hub system, and now merger mania is possibly going to, in many cases, eliminate or lessen competition. I do not think American-TWA is one of those mergers. According to your written testimony, Mr. Levine, you agree that there is not much hope for St. Louis if TWA goes under and there is no one willing at this time with the capability to buy TWA and to protect the jobs that are there and the service that is necessary at a very large city in our country.

So I would just ask you, in light of all of the questions that we have heard, mostly to Mr. Leonard and Mr. Levine: What is your alternative? I mean, if you do not think that American and TWA merging is going to be in the best interests of this country, the State of Missouri, and the employees, what would you suggest is a better option? Second—I will just ask one question and hope that you can answer them in the context of the mergers that are being looked at and already contracted for—what is your alternative to these mergers?

How are you going to increase competition when there are no willing competitors ready to step up?

Mr. LEVINE. I thought I was quite clear both in my verbal testimony and my written testimony that I do not object to the American-TWA merger on public interest grounds. Any comments I have been making are addressed to whether it might or might not be a great business transaction for American. It is American's job under the U.S. economic system to figure out what is a good business transaction for them. So I am not suggesting an alternative to that transaction because as far as I am concerned I do not think there ought to be a public objection to that merger.

As to the larger transactions that are the much more important issues here today, I would not permit these mergers. I would let US Air and its unions negotiate out US Air's cost disadvantages, which in my judgment are manageable. US Air in my judgment is not a failing company. It is a company which has faced hard choices and is ducking them on both management and the union side and hoping that this transaction will bail them out of those choices, and in my opinion they should be left to work their way in the competitive marketplace.

I think the East Coast infrastructure is an emergency issue that needs to be dealt with. I have a variety of suggestions that probably time does not permit my making here, but——

Senator HUTCHISON. May I just interrupt you before you go to that second point. Do you think it would be fair to United and US Airways to allow this merger to go through, but not theirs? Would that set up a competitive——

Mr. LEVINE. AA–TWA?

Senator HUTCHISON. Yes.

Mr. LEVINE. Absolutely, it would be fair. The antitrust laws as far as I am concerned are about preserving competition. They are not about the question of whether you are being nicer to one company than another. They are addressed to preserving competition. In my judgment the TWA-American merger does not threaten competition because TWA will not be here to compete and in my judgment it is unlikely that anyone else will attempt to run a hub at St. Louis, so I do not see an effect on competition.

In the case of US Air-United on its own or with American, I think both of those transactions ought to be disapproved. That is my personal view, unpaid for by anybody. I would allow the process which has been going on to continue. The fact is that Delta and Northwest and Continental have all been gaining market share on American and United. That is a process that in my judgment United and American seek to arrest by building a fortress wall around the East Coast which will not be duplicable by anybody else, and I do not think that is something the government should allow.

Senator HUTCHISON. Mr. Leonard?

Mr. LEONARD. I think if you look at it in context there are four successful new entrant airlines, highly successful new entrant airlines. We are one. We were formed because of Eastern's bankruptcy. The only way that we got started was Eastern vacated gates in Atlanta and we took those over. We could never start today and get to where we are. It would be virtually impossible.

JetBlue got started because the government granted them 75 additional new slots in order to do that. Without those slots, they could not have gotten started.

Southwest was protected by the Wright Amendment for a very, very long time. That gave them time to build a fortress in Texas and then grow that nationwide and now it is a very, very tough competitor all over the country.

The last is Frontier. Frontier was created because Continental abandoned gates in Denver and they were able to get a foothold in Denver and build a network.

Very few of the other new starts are successful because they do not have network. The same principles that apply to Mr. Carty apply to us. If you do not have a network, you are not going to be able to survive.

So what I would recommend, which is what I have been recommending, is that as part of national policy, any time a merger occurs, big or small, that a certain percentage of the gates and slots at these slot-controlled airports and gate-constrained airports should be forced to be relinquished back to a pool and reassigned to new entrant airlines.

It took us a year and a half to get one gate at Newark, even though we could prove that there was the equivalent of 13 gates available there which were being horded by the large airlines. Well, we have been trying for 2 years to get additional gates at Philadelphia; impossible to do so up until now when we are starting to get some help. I could go on and on. Slot-constrained at LaGuardia, slot-constrained at Washington National.

So what needs to be done is for the barriers to come down, and the United-American deal that is on the table will make the barriers so high that it will be impossible for anybody to compete in the future. We need to reallocate the assets that are restraining trade.

Senator HUTCHISON. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Hutchison, and we look forward to working with you and Senator Rockefeller, particularly in the area of the air traffic control system and increased capacity. It is very popular, and I am probably one of the most guilty, to voice criticism at the airlines themselves, but if they do not have places to land and if they do not have a system that can get them from one place to another, clearly the responsibility has to be shared. I look forward to working with you and Senator Rockefeller as we address those important aspects.

I would remind the panel that Senator, now Secretary, Mineta was part of a panel a few years ago that predicted pretty much what was going to happen to aviation in America, and we as a nation and as a Congress were unable to come up with solutions and we are there. So I think the issue is serious. I think it will dominate a lot of the work of the Commerce Committee, and I look forward to working with you.

Senator Carnahan.

STATEMENT OF HON. JEAN CARNAHAN, U.S. SENATOR FROM MISSOURI

Senator CARNAHAN. Mr. Chairman, like Senator Allen, I want to apologize to you for my late arrival. I was at the National Prayer Breakfast, where I hoped that my participation would also serve the national interest. However, it did not qualify me for the early bird exemption.

The CHAIRMAN. Thank you, Senator Carnahan. I am sure it was well spent.

Senator CARNAHAN. Thank you. With your permission, I would like to submit my full remarks for the record.

The CHAIRMAN. Without objection.

Senator CARNAHAN. I also want to commend Senator Bond and Governor Holden for their strong commitment to the TWA acquisition.

As I mentioned during Secretary Mineta's confirmation hearing, I share the concern of many Members of this Committee regarding the consolidation in the airline industry and the resulting reduction in competition. However, I want to emphasize again, as it has been emphasized today already, that I believe that the American Airlines acquisition of TWA is distinct from the other mergers that are pending. TWA is a financially distressed firm. It cannot be saved or revived without the intervention that is proposed by American Airlines.

But I am concerned about the future of TWA's employees and their families, and to date American's proposal to purchase substantially all of TWA's assets is the only scenario I have seen that assures continued employment opportunity for TWA employees. Should this venture fail, I can only imagine the heartache of the families of these 20,000 employees who have struggled so long in the hopes that they could find a workable solution.

So I urge my colleagues here on this Committee to consider the unique circumstances, these unique circumstances, when assessing this proposal.

I have one question I would like to ask of you, Mr. Carty. I was extremely pleased to hear you say, as well as Mr. Compton, that you plan to offer employment opportunities and to maintain the hub in St. Louis and to also maintain the health and the travel and the retirement benefits. But I would like to inquire about the overhaul facility in Kansas City. I know you have two overhaul facilities already, one that is far larger than our Kansas City one, one that is about the same size. Do you see the need for keeping the one in Kansas City?

Mr. CARTY. Most definitely, Senator. I am glad you asked. One of the real hidden assets from our perspective in the TWA transaction is in fact the Kansas City major overhaul base. This country and this industry is going to be facing a shortage of maintenance capability both in terms of facilities and, just as importantly, in terms of skilled professional mechanics. Kansas City in one fell swoop gives us both.

We will have, as a consequence of this transaction, 200 more airplanes to do major overhauls on and Kansas City can accommodate those 200 and it can accommodate more than that. So as we continue to grow the company, I would expect we will be growing the Kansas City maintenance base, not simply sustaining it. That to us really is one of the unique aspects of this deal.

Senator CARNAHAN. Thank you, Mr. Chairman.

[The prepared statement of Senator Carnahan follows:]

PREPARED STATEMENT OF HON. JEAN CARNAHAN, U.S. SENATOR FROM MISSOURI

Mr. Chairman, TWA has one of the most distinguished histories in the airline industry. Many of you may not know this, but having been in service for over 75 years, Trans World Airlines is the oldest continuous name in U.S. commercial aviation. As a Missourian, that is something that I take great pride in.

Unfortunately, however, after nearly two decades of financial difficulties, including the current string of 12 consecutive years without posting a profit, TWA has reached the point where it is no longer able to survive independently.

The company's mounting debt and poor credit, coupled with continued problems associated with a prior separation agreement with former owner, Carl Icahn, caused irreparable damage to the airline. Ultimately, these problems became too burdensome to overcome, even in light of the exceptional efforts of TWA's management and employees.

Earlier this month, American Airlines proposed to acquire substantially all of TWA's operating assets. TWA's board of directors approved American's proposal. While I am saddened by the fact that St. Louis will lose it's hometown airline, my overwhelming concern is for the jobs of the more than 20,000 TWA employees and their families. Officials at American Airlines have assured me that they plan to offer employment to virtually all of TWA's contract employees—including the employees at TWA's overhaul base in Kansas City.

While continued employment opportunities for TWA employees is foremost among my concerns, I was similarly fearful about the negative impact that TWA's liquidation would have on the rest of the state's economy. St. Louis' Lambert International Airport, where TWA is headquartered, has an annual economic impact of $5 *billion* on the region. Having a "hub" in St. Louis is critical to maintaining the region's economic vitality. American has assured us that they plan to use St. Louis as a hub.

American's proposal is the only scenario I have seen to date that provides the key assurances in terms of maintaining jobs, the overhaul base in Kansas City, and St. Louis as a hub.

Therefore, Mr. Chairman, even in light of my general concerns about consolidation in airline industry and the potentially adverse impacts it could have upon consumers, I view American Airlines' proposed acquisition of TWA as wholly separate and unique from the other mergers which are currently pending. I urge you and the other Members of the Committee to do so as well.

The primary difference with the American/TWA deal is that, as I mentioned, TWA is a financially distressed firm. With most of its assets used as collateral for earlier loans, the airline is unable to borrow any additional funds. Furthermore, record-high fuel prices have ultimately driven TWA into bankruptcy. In fact, were it not for the $200 million of debtor-in-possession financing that American provided, TWA would not even be operating today. Because of TWA's precarious financial situation, it is also critical that this transaction be dealt with swiftly.

During the bankruptcy court proceeding last weekend, the judge in the case held up a thick folder of papers and said, "These are letters and forms from TWA employees. And they all support the transaction." My office has been similarly inundated with calls and letters from TWA employees imploring me to help save their jobs.

As a Senator from Missouri, I cannot overlook the damage—particularly the loss of jobs—that TWA's closing would have on my state and on the nation as a whole. I hope that these circumstances will be taken into account when evaluating the various deals that are before us. Mr. Chairman, thank you for convening these hearings, and I look forward to hearing from the witnesses who are here today.

The CHAIRMAN. Thank you very much.
Senator Snowe.

STATEMENT OF HON. OLYMPIA J. SNOWE, U.S. SENATOR FROM MAINE

Senator SNOWE. Thank you, Mr. Chairman. I appreciate your scheduling this hearing today. Unfortunately, we are all too often having hearings on this subject, and for good reason, because obviously, as you have heard from so many of my colleagues here on the Committee, there are some serious concerns about the direction of the aviation industry.

I always like to mention the fact that when I was elected to Congress and began commuting on a weekly basis in 1979, we were still in a regulated environment. The current environment does not resemble the kind of an environment today in the airline industry. Obviously, a lot has changed. For those of us who represent rural states and rural communities, we are all the more concerned about the direction that these mergers portend.

Ultimately, we are going to see, I suspect, three airlines that will dominate 75 percent or more of the market here in the United States. Obviously, we are seeing competition undermined. We are seeing higher prices. We are seeing diminished service to smaller communities, like the State of Maine, in addition to what Senator Dorgan indicated in his remarks. So that is the direction and that is the concern.

I would like to ask, Mr. Johnson, in your original proposal with United you mentioned the fact in the creation of DC Air that you were going to maintain service to the communities in the Northeast, that you were going to continue essentially the same service. Do you intend to maintain that commitment in your merger with American?

Mr. JOHNSON. Yes, Senator. I think the cornerstone of what DC Air is proposing is that the communities, the small communities, particularly those in Maine and other places along the Northeast Corridor, will continue to receive the service that they were receiving for the past 40 years under US Airways, but with some significant differences. We believe we will bring lower costs and therefore lower prices because of the nature of our operation as significantly different than US Airways.

We will bring the advantage with American of the frequent flyer miles that will be very attractive to passengers traveling on DC Air from Portland, say, who will then have AAdvantage miles that will take them throughout the American system. We will move very quickly to a full jet/regional jet service that will have the right number of seats for the capacity that we are flying.

As I said before, if these slots at Reagan National were to be distributed out, as some have suggested, it is very likely that many of these small communities that are not profitable in the context of a hub system would lose direct nonstop jet travel to Reagan National. As I finally indicated——

Senator SNOWE. That is a big "if."

Mr. JOHNSON. There are people advocating that that is the best way to dispose of these slots, rather than to create DC Air which will continue to serve these 45 communities, which I think is in the best interest. Furthermore, I would say that probably of all the carriers at this table I would be the only carrier to sign a consent decree committing to fly to those communities and no other communities.

Senator SNOWE. What about American's commitment in that regard in providing air service?

Mr. CARTY. Senator Snowe, our commitment, as I said earlier, is to let Bob Johnson run this company and be absolutely supportive and be a minority investor, unless he wants help or advice.

Senator SNOWE. So you would support that approach?

Mr. CARTY. We are prepared to invest in a company that has made that kind of consent decree commitment.

Senator SNOWE. There was an article recently concerning this proposed merger and it talked about how, as for hub to hub concentration concerns, on five routes where only one carrier would operate after the merger, American agreed to serve those routes for a long period of time whether they make money or not. Those routes are Charlotte to Chicago, Pittsburgh to Washington Reagan, Philadelphia to Denver and San Francisco or San Jose Airport.

I could not help but think, if Charlotte, Pittsburgh, and Philadelphia's hubs could not make money, I do not know how Portland, Bangor, or Presque Isle could. I think that is a central concern. As we see fewer and fewer airlines serving America, and certainly serving our part of the country, how is it that we are going to get better customer service how is it we are going to get lower prices or fair prices, how is it we are going the get better equipment, because that has not happened?

US Air has really done a good job in serving Maine and I certainly appreciate what they have done for our State, at least in providing direct service and continuous service. But that has been the exception for our part of the country and not the norm. That is what concerns me, because we have no control over the direction or the prices or the type of equipment. I do not see how that is going to get better in the future with fewer airlines.

Mr. CARTY. Senator, I think you make a very good point, but I would say this to you. I think the challenge of serving small communities economically lies before us regardless of whether or not there is further consolidation or not. I think it is almost an independent issue, but an important one. As I said in my earlier testimony, I really do believe that if we want to have the kind of service in this country to these small communities that they want and they deserve if they are going to participate in the economic benefits of what the U.S. economy is doing, we are going to have to relook at the essential air service system, because I think we are going to have to find a way to subsidize that service and do so until such time as those communities build enough critical mass to be successful on their own.

Senator SNOWE. Well, you make an important point, Mr. Carty, because in northern Maine, in Presque Isle, Maine, we had to invoke essential air service for that reason, because there would be no airline service to northern Maine otherwise. Twenty years ago they had 727's. Now you have to rely upon the essential air service program in order to have any kind of service, and you cannot get there from within Maine. You have to go to Boston in order to get to northern Maine. So that is where we are today. That is the state of the aviation service within Maine, and a lot has changed.

Frankly, I see some other policies that need to be addressed As Ms. Hecker has mentioned, I have asked for a GAO study on the whole issue of regional jets. Portland, Maine got short-changed at LaGuardia recently. Delta was making a major investment of a billion dollars in regional jet service and, guess what, the one direct service from Portland to LaGuardia was based on one of the many slots eliminated, at a time when a major airline was investing in regional jets, which we are encouraging as a policy in this country. Yet, when it comes to being able to compete with the populated areas with the bigger aircraft, we will never be able to stand on a level playing field. That is the other dimension to this entire problem.

When I look at how much all Americans have invested in commercial aviation, it is an incredible number. I asked my staff to look it up and since 1918 American taxpayers have spent $155 billion for infrastructure, for air space, for equipment, and so on and so forth. So not every American benefits from all of this investment, but ever American pays for it.

So we clearly have been on the wrong track and it is one that I think that we have to consider in the future in terms of perhaps conditioning some of these arrangements to ensure that all Americans in fact do benefit.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Snowe.

Senator Rockefeller.

STATEMENT OF HON. JOHN D. ROCKEFELLER IV, U.S. SENATOR FROM WEST VIRGINIA

Senator ROCKEFELLER. Thank you, Mr. Chairman. I will be very brief. I will not even ask a question.

A couple things occur to me. No. 1, as the Chairman of the Committee knows, I support the US Air-United-DC Air arrangement, and I always have and I always will. It is very easy for me because US Air does not provide the kind of service I would like to see in West Virginia and Bob Johnson and DC Air is going to do it, and he is going to do it with something called regional jets.

It has been so long since I have heard the sound of a jet that I look upon him as salvation for our economy. So that is not very hard for me. You know, US Air goes up and down, United goes across, and they intersect in DC Air. Bob Johnson is right about the slots. They would all go elsewhere. So that is one point.

The second point, I do not start off at all unfriendly to the second merger, because again, is it a merger or is it a bailout? It is something which needs to happen and if it did not happen where would there be any sense of increased competition? There would not be. So it needs to happen.

Now, that makes three or four or whatever it is very large airlines and therefore offends the sense of competition. But in dealing with reality, competition to me is when I can get somebody from, let us say, Dallas or Santa Barbara to get into Washington and then to get to West Virginia in something called a regional jet, because if they do their whole attitude about West Virginia, either locating a business there or coming back there, wanting to meet with me or deciding I do not exist, a lot of that is formed by whether or not they come in on a regional jet or a prop plane. So I support that.

Second—and I think I support the second one, too, because of the backup that you have each indicated, that Bob Johnson and Don Carty have indicated, in terms of the way you view each other.

The last point I want to make, Mr. Chairman, is something that Don Carty mentioned in conversation. That is—and this is not a good comparison, but it is the only one I could come up with for the moment—in the telecom business we passed a law—and the telecom business, that is the way people communicate. Well, so is flying. I think flying, aviation, is now coming to the point where it is more important than highways for America's future. Telecom obviously is huge.

But in telecom we say: Oh, you cannot just have comparable service; you have got to have similar service at similar rates, and that is the deal. It is in the law. Now, that does not apply just by definition of economics, passenger loads and everything, in aviation and I understand that. But that is why I like the idea of us as a Committee, but more importantly the industry as an industry, taking what you referred to, Mr. Carty, as a very special effort to look at the whole question, not just of essential air service, which I now sort of associate with airports which are barely open—it is almost like a death wish—but rather taking rural—and you have got to get people out of the rural areas to get them to your hubs, to get them into your mainstreams, around the country and around the world, and Bob Johnson is going to help you do that, up and down the East Coast.

But I think that the idea of the industry, industry leaders taking the lead to get together to figure out what do we do about these rural areas, because if you are born in a rural area you are no less of a person than if you are born in New York City or some huge city like Rockland. There is a real principle involved here about human beings.

So I would just really encourage you to do that. We need to do it, but you need to do it. It is like customer service. We can do it, but you probably will not like it, and therefore you have got to do a good job at it or else we will do it. I think the same applies on this.

That, Mr. Chairman, is my statement.

The CHAIRMAN. Well, I thank you, Senator Rockefeller.

I want to thank the witnesses for their patience. This has been a very long hearing. Senator Allen would like to ask another question, so the hearing will be even longer.

Senator ALLEN. I thank the chairperson and the witnesses. I would like to put my statement in the record.

The CHAIRMAN. Without objection.

[The prepared statement of Senator Allen follows:]

PREPARED STATEMENT OF HON. GEORGE ALLEN, U.S. SENATOR FROM VIRGINIA

Mr. Chairman, thank you very much for calling this hearing on such a critical and timely issue. This issue of market consolidation is not unique to the airline industry, but is being experienced across our economic landscape as the expansion of international trade and gains in reducing unit costs and improving labor productivity forces companies to seek greater economies of scale wherever possible. This consolidation is evident throughout the transportation industries, from steamship companies, with the purchase of SeaLand by Maersk from CSX, to railroads, and to automobile manufacturing. But not many passengers travel by steamship these days, and so it doesn't become a matter of general public discussion as does airline consolidation.

I share with you, Mr. Chairman, as I believe every Member of this Committee does, the absolute commitment to seeing that the United States commercial aviation market is competitive, safe and efficient. Safety and efficiency are truly the providence of the Federal Aviation Administration, and this Committee has a lot of work ahead of it to try to fix the severe stresses the Air Traffic Control system is experiencing.

And on the issue of competition, the Sherman and Clayton Acts lay down, as you well know, clear guidelines under which the Department of Justice must analyze any potential merger that could impact competition within an industry. For the last seven months, I understand the Department of Justice has been intimately involved with the parties to the United-US Airways merger, and that this process will most likely be continuing into April of this year. I also understand that the Department of Justice has been raising a number of concerns regarding the proposed merger, concerns that have required significant changes to the original merger proposal, and that this merger proposal is by no means a done deal.

While I was Governor of Virginia, I learned first-hand how complex and time-consuming the regulatory review process can be. For a $13 billion deal like that being proposed by United and US Airways, and now also American Airlines, I can only imagine how much more so it must be here. I raise this issue because throughout the testimony and statements here today, I have not heard much about the inadequacy of the current merger antitrust review process. In fact, I can remember the strong objections many Members of the Senate have taken to other antitrust measures initiated by the Department of Justice, most noticeably the case against Microsoft, or even the hostility evinced by Justice to the initial forays by Northwest and Continental to some type of merger. Before I came here, my impression was that many Senators believed Justice was TOO aggressive in antitrust enforcement, not too lax.

Given that, I think that we need to move cautiously before we pre-judge the decision making process underway at the Department of Justice. The fact of the matter is that Justice could still deny this merger application and that the concerns raised today may very well be moot.

But meanwhile, there is something that is proceeding apace, regardless of what Justice decides. And that is both TWA and US Airways are in unsustainable financial situations. US Airways lost almost $300 million last year, more than one-third of that in the last quarter alone. TWA has gone through bankruptcy twice, and I understand if not for the proposal with American, would have had to go into liquidation very soon.

Such an uncontrolled demise would be catastrophic for the communities served by these airlines. Without some type of controlled transfer of aircraft, routes, gates, airport slots, reservation systems, existing tickets, and passenger reward programs, air travelers will be left holding the bag with little recourse except to accept their personal losses and inconvenience. Meanwhile, tens of thousands of highly-paid technical employees will be abruptly laid off, and communities could very well find themselves with extremely limited, or even no air-service. Forcing such an outcome would be, in my opinion, irresponsible and ultimately more injurious to airline competition than an orderly transition overseen by the antitrust division of the Department of Justice.

So I guess that's the main point I want to make today, Mr. Chairman; the status quo is not sustainable and some type of major change in the airline industry is inevitable. TWA is on it's last gasps, and US Airways is finding itself in an increasingly untenable financial situation, one that I do not believe can be maintained for any significant period. Therefore, in my opinion, the question becomes how will such inevitable change be managed?

I am heartened by the commitments United has made to the communities currently served by US Airways, as well as to the US Airways employees, especially for the communities and employees in Virginia. No one will be laid off, fares will be frozen, and service to all existing communities will be maintained. In addition, a new low-cost carrier will come into one of the highest cost airports in the country, Reagan National. Given the realities we face, this seems like an exceptionally favorable outcome to a bad situation for my constituents.

However, I realize that significant issues will still remain regarding the competitiveness of the US airline industry, issues that have their roots in market structures that were established before, or independently of, the current financial woes that beset TWA and US Airways. Such issues as hub dominance, market exclusion, potentially predatory behavior, and the impact of new technologies such as regional jets and Global Positioning System, all deserve full analysis, and I look forward, Mr. Chairman, to working with you to ensure a viable, competitive, safe, and efficient airline market.

The CHAIRMAN. Without objection.

Senator ALLEN. Thank you.

Senator ROCKEFELLER. Mine too.

The CHAIRMAN. And Senator Rockefeller's.

[The prepared statement of Senator Rockefeller follows:]

PREPARED STATEMENT OF HON. JOHN D. ROCKEFELLER IV, U.S. SENATOR FROM WEST VIRGINIA

Mr. Chairman. This Committee spent three days in hearings on this subject last year, another day debating S. Res. 344, which effectively, and in my view inappropriately, denounced the United Airlines-US Airways-DC Air deal, and many more hours analyzing the transactions' impacts on our communities and on competition in general. The Departments of Transportation and Justice have done and are doing the same, though in much more detail and according to strict legal and economic standards. In the end, I hope that these transactions will be approved, subject to the modifications and conditions that the Department of Justice requires to ensure competition.

I look at these various transactions from two vantage points—one as the Senator from West Virginia in dire need of better air service, service that is a life line to the outside world; and a second as the Ranking Member of the Aviation Subcommittee, with a desire for a competitive, dynamic, and safe national air transportation system.

What I see for my State in this deal is the equivalent of a seat upgrade, from coach to business class. We all are aware that US Airways does not have a stellar record of service. Its commuter affiliate network which today provides most of its service to West Virginia is, frankly, not doing the job. We have had countless meetings with our airport directors, the commuter carriers, and others to try to improve the situation. US Airways management has tried to work with us, but hasn't had the resources to take any significant action.

US Airways may not technically be a "failing company" under the antitrust laws, but at the bottom of its service food chain it certainly acts like one. And by virtually any measure, US Airways is a company with a deeply troubled future. In a year when a carrier like Delta had earnings of $897 million, US Airways lost $269 million. Perhaps they should have done many things differently, but the fact is they did not grow substantially during the boom years of the late 1990s and have not succeeded in reducing their costs. US Airways still has the highest costs per available seat among the major carriers. Despite controlling two so-called "fortress hubs" in Charlotte and Pittsburgh, where DOT says the airline enjoys incredibly high yields, US Airways is not making money.

The bottom line is that the problems for this carrier are real, and they are affecting the economy and the future of my State and of other small communities in the East.

Along comes one of the two biggest carriers in the industry with a deal for US Airways, and the creation of a new air carrier, DC Air. All of a sudden, we move up to business class. United will offer us more connections to more cities and, hopefully, better schedules, more flights, and generally better service. United, as we all are painfully aware, had its own set of customer problems last year and it must improve its performance, but small communities in West Virginia and across the country need access to a major network carrier to survive. DC Air is the icing on this cake. DC Air offers us a true entrepreneur and committed new airline executive, who is willing to invest his time and a substantial amount of his personal funds to create a new carrier. DC Air has a business plan that is all about serving small cities out of Reagan National Airport better than they have been served in years.

Now, DC Air and United have taken seriously the competition demands and challenges of the Department of Justice, and Members of this Committee. They have found a serious, significant competitor—some would say United's single biggest competitor—and divested parts of the original deal. Last year Mr. Johnson committed to us that he and DC Air would be independent of United Airlines, and now he's followed through on that commitment by selling to American Airlines a 49 percent share in his airline. The American Airlines marketing arrangement and possible code-sharing place DC Air squarely independent of United. And American's agreement to start service in 5 critical markets that stood to lose competition, plus the splitting of the highly lucrative shuttle service on the East Coast, seem to me only to strengthen the competitive nature of this deal.

Still to be determined by DOJ is whether or not American is obtaining too much in the way of gates and slots in the Northeast. American already has a substantial presence at Boston (14.2 percent), at JFK (21.7 percent) and at LaGuardia (16.6 percent). The TWA-American deal and United's sale of US Airways assets to American will change those figures significantly. American will get gates and slots in New York, and gates in Boston. American and United may end up creating a town that's only big enough for the two of them, leaving the other major carriers with too little to build and maintain an airline around. DOJ will have to be persuaded not only that the American-United transaction addresses its concerns with the United-US Airways merger, but also that it doesn't create any new competitive problems, and I look to them for a sound decision.

Market by market, airport by airport, United's takeover of US Airways has consequences—some good, some bad. The good news is that West Virginia gets an increased presence by United, gets American Airlines back in the state for the first time since deregulation, and gets added competition and a long-term service commitment from the best new regional carrier to come along for us in a very, very long time—DC Air.

Given the fundamental decisions on these mergers are, by law, out of our hands, I think the real question for this Committee and this Congress, I think, is whether airline consolidation creates an opportunity to take affirmative steps to actually improve service and competition. For the state of West Virginia, I believe these deals do that on their face. For other communities it may take some other action—perhaps a whole new approach to rural air service and a more concerted effort to break down any remaining barriers to entry and promote start-up carriers. This is the time to think creatively and work cooperatively to ensure that the public interest comes first in aviation. I look forward to working with my colleagues to do that in this new Congress.

Senator ALLEN. In reading all this, Mr. Chairman, I think the key to the lower cost for customers is competition, not necessarily in the emergency situations in rural areas, but in places like Richmond. There was no doubt when I was Governor we were trying—we put billboards up to get Southwest, outside of Southwest Airlines headquarters in Texas, to come into Richmond. AirTran provides that in some of the facilities that you should come to in Virginia, but we do need to get better competition for lower prices and better service.

To how that is all done, it may be predatory behavior, whether it is the gates, whether it is the hub dominance, and so forth, clearly that is not going to get figured out right today. But that is something that this Committee clearly needs to look at.

I think I am in support of the US Air situation. I think they are in an untenable financial situation and that is an unfortunate situation as far as I am concerned, since US Air is headquartered in Virginia.

The TWA situation, clearly to have American take over TWA is very important. You will not find in a bankruptcy sale or liquidation anybody saying: Gosh, we will take over and pay the medical, health and dental benefits, and those obligations. So that is a slightly different situation. TWA is just further along the line in economic stress than US Air is, but US Air in their view will soon be there.

Now, Senator Boxer and Senator Carnahan talked about various employees and so forth, and I have spoken with Mr. Compton about their airline reservation center in Norfolk. When I was Governor we were in competition to get that airline reservation center in Norfolk, and that means a lot. I would like to hear Mr. Carty's views as to—and I know you have airline reservation centers. I think they are in Chicago and St. Louis, I think were the other ones. How are you going to analyze the airline reservation centers as to which jobs? I know they are unionized jobs and I know they are protecting their jobs. I would like to see their jobs staying in Norfolk as opposed to saying, you can keep your job but you have to move to Illinois.

Mr. CARTY. Senator, obviously with a bigger airline we are going to need more res positions than we have today, so it is our expectation that we will need all the capacity that TWA currently has. I am told, as an aside, by Bill Compton that the res operation in your state is the most efficient one in the St. Louis system. That will certainly bear on our thinking.

But I should mention one thing. That happens to be a group of employees, the only group of employees, who are unionized at TWA and are not unionized in American Airlines. So it is not clear when the smoke clears that they will be unionized. But nonetheless, we do intend to employ those employees and we do intend, if all that Bill has told me about the Virginia res office is true, to operate the Virginia res office.

Senator ALLEN. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Allen.

Again, I want to thank the panel for their patience. I think it is an indication of the deep interest that not only this Committee but the entire Senate and American people feel about this issue. I thank you for your participation and I think you have been very beneficial in helping us be better informed as we address not only this particular issue, but the broader issues that have been addressed in the hearing.

Thank you, and this hearing is adjourned.

[Whereupon, at 12:39 p.m., the Committee was adjourned.]

APPENDIX

PREPARED STATEMENT OF HON. SAM BROWNBACK, U.S. SENATOR FROM KANSAS

Mr. Chairman, thank you for holding this hearing on this important issue—I think everyone noticed at last week's confirmation hearing of Secretary Norm Mineta, that aviation issues are at the forefront of everyone's minds, whether it is mergers and acquisitions, delays and congestion, competition and pricing, or even customer service. The Chairman and the new head of the Aviation Subcommittee, Senator Hutchison, have their work cut out for them in this Congress.

I come from a rural state, which has no hub airports, and has a lot of rural communities with little air service, or no air service at all. Many of our communities are dependent on essential air service. I share my colleague's concerns that consolidation in the airline industry will mean higher prices and fewer choices for consumers. If you think fares are high in hub airport cities, try coming to Wichita, Kansas, where last night, the walk up, round trip, same day return fare to Denver ranged from $1,069 to $1,643, and the cheapest flight goes east to Kansas City, before going west to Denver. In fairness, I must point out, the walk up fare between Wichita and the number one destination out of Wichita, Dallas—Fort Worth, ranged from $349 to $369. But if you think fares are high in hub cities, try going to Goodland or Great Bend, Kansas which have lost their essential air service, and flying is not an option at all.

But as I travel my home state, the number one aviation issue among my constituents is not fluffy pillows or whether the gate agent was helpful or not. My constituents are sick of flying because of flight delays, cancellations and congestion at our airports. We have a capacity crisis in our nation's aviation infrastructure, and my constituents have caught on. They fly defensively, avoiding if at all possible certain airports because they are notorious for delays.

We must increase the capacity on the ground at our nation's airports. We must build more runways and build them faster than we are doing now. The new runway at Memphis, took, what, 12, 16 years to complete? That is absurd. The crisis is here. It was last summer, and it was the summer before that, and we still have done nothing about it. I intend to do something about it, and I look forward to working with the panelists and my colleagues on this Committee to see that at least this one aspect of our nation's aviation capacity crisis is addressed by this Congress.

PREPARED STATEMENT OF HON. RICK SANTORUM, U.S. SENATOR FROM PENNSYLVANIA

Thank you Chairman McCain, Senator Hollings and Members of the Committee. I appreciate the opportunity to submit testimony today on the impending airline mergers. I am particularly interested in these mergers as they relate to jobs and services for my constituents and as they impact competition in the airline industry.

With regard to the United-US Airways merger, I made it clear when the merger was first announced that to gain my support the airlines had to address my two principal concerns—protecting existing jobs in my state and continuing plans to build a new maintenance facility in Pittsburgh. Since that time, United Airlines Chairman Jim Goodwin and US Airways Chairman Stephen Wolf announced their willingness to make good on both of those promises.

In particular, I was very pleased that United Airlines committed to the long-planned expansion of the maintenance facility in Allegheny County. This project is not only important to the Commonwealth of Pennsylvania; it is critical to the thousands of maintenance workers that depend on these jobs to support their families. I believe the United-US Airways alliance will benefit the people of Pennsylvania and consumers.

Knowing there are still critics of the United-US Airways merger, I respectfully request that you consider the alternative. Just a few weeks ago, US Airways reported that high fuel prices and expanding low-cost and network carrier competition combined to produce disappointing financial results for the company—a net loss of $269 million for the year 2000. Absent this merger, US Airways would be in dire financial straits and jobs at US Airways would be in jeopardy. Previous air carriers didn't have the opportunity that US Airways has today. Consider the employees of Pan Am, Eastern and Braniff and how the states where they operated have been impacted.

Without the merger to preserve US Airways' service network, I question if Pittsburgh, Philadelphia and smaller communities across my state will continue to get the kind of service that they need. The merger would not only ensure but expand the service to and from the Commonwealth of Pennsylvania.

I understand that looking beyond the United-US Airways merger there is some concern about the longer-term impact on competition in the airline industry. However, recent economic studies demonstrate that airline mergers can have tremendous benefits for consumers—in addition to saving tens of thousands of highly skilled, high paying jobs.

Specifically, airline consolidation can increase travel convenience for consumers. In the merger of US Airways with United Airlines, travelers would be able to reach more destinations without switching airlines. Not only is direct travel more convenient in terms of connection times, baggage handling and frequent flier miles, it is also on average 55 percent cheaper than switching airlines.

I believe the airline mergers in question are a step towards replacing fragmented regional networks with truly national networks and creating local and nationwide competition. The end result would be good for my constituents and good for our nation's travelers.

Thank you, Mr. Chairman.

February 7, 2001

Hon. JOHN MCCAIN,
U.S. Senate,
Committee on Commerce, Science, and Transportation,
Washington, DC.

Dear Mr. Chairman:

I am writing to express my strong support for the proposed merger between Trans World Airlines (TWA) and American Airlines. As the Congresswoman representing Missouri's fifth district, which includes most of Kansas City, I feel it is quite important to share my thoughts with the Senate Committee on Commerce, Science, and Transportation on how important this proposed merger is to my constituents as well as to my State.

I understand that you and many of your colleagues have concerns with the consolidation process in the airline industry. Such consolidation threatens to reduce air service to smaller communities as well as decrease price and service competition. I share these concerns as well, but I know the TWA-American Airlines merger is different. TWA cannot survive in today's current market. Without American's debtor-in-possession financing, TWA would go out of business immediately. Its assets would he liquidated, its employees out of their jobs, and St. Louis would no longer be a hub. The economic impact to Missouri's, Kansas City's, and St. Louis' economies would be quite substantial.

TWA currently has 20,000 employees. In my home state of Missouri, almost 13,000 people are employed by TWA, including 3,500 in Kansas City. Many of TWA's Kansas City retirees and employees reside in my district. Under the agreement between American and TWA, virtually all of TWA's contract employees will retain their jobs and TWA's retirees will be provided medical and dental benefits through American. In addition, American has agreed to keep the hub at St. Louis' Lambert International Airport and potentially expand the overhaul base in Kansas City. Retaining St. Louis as a hub and the overhaul base in Kansas City is critical to the Kansas City metropolitan and St. Louis regional economies.

I respectfully request that you and the Members of Senate Commerce Committee view the American-TWA merger in a different light from the merger proposed by United Airlines and U.S. Airways. TWA only has 3.9 percent of the market share and would go immediately out of business without American's proposed buy out. The only way to ensure that thousands of long term employees of TWA do not lose their jobs in my state of Missouri and throughout the country is for this deal to be approved. It is my hope that the Justice Department does not prevent this transaction from going forward, and I would respectfully urge my Senate colleagues not to take any steps that would jeopardize this effort to save the jobs and services of TWA.

Best personal regards,

KAREN MCCARTHY

PREPARED STATEMENT OF HON. THOMAS M. REYNOLDS, CONGRESSMAN FROM NEW YORK STATE

Mr. Chairman and Members of the Committee, thank you for the opportunity to testify before the Committee today. I represent the 27th district of New York State, including the rural and suburban areas surrounding the upstate cites of Rochester and Buffalo.

Both these areas are working to rejuvenate their local economies: working to tie academia and industry to a technology base to create a pro-growth atmosphere that encourages job creation and retention.

In seeking to foster economic development, experts often cite a number of factors as disincentives to new business development in the region, including high taxes, regulatory burdens, energy prices and astronomical airfares.

Pending mergers and acquisitions in the airline industry present the prospect that my constituents, who currently pay some of the highest airfares in the nation, will continue to find themselves locked into these high fares in virtual monopoly markets. It is highly unlikely that the conditions of current proposals—including the proposed sale to DC Air of US Airways' valuable slots at Reagan National—will provide any prospect of relief.

Mr. Chairman, in your opening statement before the July 27 hearing of the Committee on antitrust issues in the airline industry, you quoted the "father of airline deregulation," Professor Alfred Kahn: "If I had to choose between encouraging low-fare entry like the kind that has benefited the public with low prices, and the unencumbered ability of major airlines to respond to low-cost competition . . . I will pick the first every time." It is just this type of low-fare competition that has been a saving grace for the upstate New York economy thus far, and it is just this type of competition that we desperately need more of.

Southwest Airlines currently provides service between Buffalo and Baltimore-Washington-International Airport. JetBlue Airways provides service between New York's John F. Kennedy International Airport and both Buffalo and Rochester. The low-fare service these airlines provide upstate New York has been a successful first step in bringing greater competition to our marketplace. These carriers as well as others, such as AirTran Airways and Sun Country Airlines, have expressed an interest in bidding for assets at Reagan National with the intention of providing low-fare service to upstate New York. Without such a consumer-friendly arrangement I'm afraid that I agree with your statement, Mr. Chairman, that on balance, pending mergers and acquisitions will do air-travelers more harm than good.

The possible divestiture of US Airways slots at Reagan National is an opportunity to bring expanded service and lower costs to Buffalo, Rochester, and other areas of the Northeast, mid-Atlantic and Midwest. However, a transfer of these assets to a large carrier would essentially be the death warrant for such relief.

Consider for a moment, some of the elements of the massive merger deals involving American, TWA, United and US Airways:

- American will obtain from TWA 175 gates and related terminal support facilities and 173 slots. American will purchase current US Airways assets including 14 gates, 36 slots, and the gates and slots necessary for American to operate half of the DC-Laguardia-Boston (United Airlines will operate the other half). In other words, the two largest carriers in the world will work together to operate the shuttle with joint marketing agreements, frequent flyer programs, and clubs.
- American will acquire 49 percent of DC Air including additional slots (222 at Reagan National) and gates. American will gain a total of 467 slots from the transaction (173 from TWA, 36 from US Airways, 36 for the Shuttle and 222 from DC Air.)

- American Airlines will guarantee that the following routes involving current United hubs or new hubs obtained from US Airways will be served by at least two roundtrips a day for the next 10 years: Philadelphia-Los Angeles, Philadelphia-San Jose, Philadelphia Denver, Charlotte-Chicago (O'Hare), and Washington DC-Pittsburgh. To assist American's service in these markets, United has agreed to provide codesharing with American at United's dominated hubs.
- American and United have also agreed that if American enters any other transactions within four years causing American to be at least 7.5 percent larger than United, the shuttle and associated gates and slots will revert to United. Think about that for a minute—the nation's two largest competitors dividing up markets. This appears to be contrary to the spirit, if not the letter of our antitrust laws.

As a result of the disappearance of US Airways and TWA, along with the new alliance between American and United, there will be a reduction in the number of hub airports competing for traffic to small and medium markets in the Northeast, mid-Atlantic and the Midwest. Options will drop for all of these communities. Moreover, none of these mergers will create low-fare carriers. DC Air's flirtation with being a low-fare carrier has long since disappeared.

Numerous media outlets, including the Buffalo News, reported long ago that DC Air not only wouldn't promise lower airfares, but may also very well reduce seats from Buffalo to Reagan National. Neither does any independent analysis of the merger to date show DC Air to have a cost structure that is likely to allow low fares. Mr. Goodwin, Chairman and CEO of United, in a letter to me, went as far to say that the airline would realize "merger synergies" that could result in a reduction in seats to upstate New York.

The nation's largest carriers have had approximately 10 fare increases in the past 18 months. More recently, they have agreed to increase the charge of changing a non-refundable ticket from $75 to $90. It stands to reason that without increased competition, those increases will become more frequent when we have only four major carriers.

Also relevant today is the fact that a number of DOT, GAO and other studies have listed slots, gate limitations, and the computer reservation system as factors that keep new entrants out of markets. In *Enforcement Policy Regarding Unfair Exclusionary Conduct In The Air Transport Industry,* DOT reports: "to keep entrants from obtaining slots at slot-restricted airports, incumbent airlines have allegedly purchased the slots that come on the market. Incumbent airlines additionally 'babysit' slots—they use the slots in relatively unprofitable markets in order to keep from losing them to a potential entrant." Incumbent's understandable reluctance to part with slots that will give a foothold to new entrant low-fare competition is an issue that can and should be addressed through the current merger deliberations.

The consolidation of the industry at this point in time to no more than a handful of carriers will only make what is already a bad situation close to intolerable. The passage of the Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR–21) was hailed as a bill to make our skies safer, modernize air traffic control, reduce flight delays and boost airline competition. Announcing the passage of AIR–21 in the House, Transportation and Infrastructure Chairman Bud Shuster said, "Our air traffic control systems must be modernized, single airlines have gained monopolistic supremacy at many of our large airports, and flight delays and customer complaints are increasing. This legislation will go a long way in relieving our overburdened aviation system without raising taxes."

Unfortunately, the spirit of AIR–21 has been violated by events such as the FAA auction to rescind the slot exemptions granted under AIR–21 at LaGuardia (which was the subject of a recent hearing before the House Aviation Subcommittee). With the passage of AIR–21, which created incentives for carriers to serve medium and small communities with regional jets, Rochester saw the proposed number of seats to LaGuardia nearly double and daily aircraft operations triple. In addition to the proposed increase in seats and daily operations, the number of airlines proposing to serve LaGuardia doubled from two to four. However, the FAA lottery to restrict access to LaGuardia is now having a disproportionate impact on airports like those in Rochester and Buffalo that are striving to provide service options to the travelling public. While these actions threaten to undo AIR–21's success, industry consolidation threatens to permanently trap my constituents in a traveler's nightmare of high fares and poor service.

We are witnessing what may be the most significant mergers in U.S. history. These mergers would allow United Airlines and American Airlines to dominate most airports on the East Coast including Reagan and LaGuardia. New entrant carriers would be blocked from getting into these airports. Actions need to be taken to ensure that new entrants can obtain access at National and to increase operations at LaGuardia. Failing that, these mergers will not achieve the maintenance of any real competition in the marketplace and will therefore fail the consumer and fail western New York.

In closing, Mr. Chairman, I believe these mergers and acquisitions not only threaten the existence of real competition in the airline industry, but will further negatively impact on the economies of those communities which can least afford additional burdens.

Thank you, Mr. Chairman, for the opportunity to address the Committee today on an issue of such great importance to western New York and the nation.

PREPARED STATEMENT OF AIR LINE PILOTS ASSOCIATION, TWA MASTER EXECUTIVE COUNCIL

The Air Line Pilots Association, Intl. (ALPA) is the collective bargaining representative for over 2,300 pilots at TWA, and over 59,000 pilots in the United States and Canada. ALPA has represented airline pilots since 1931.

TWA's future has been in doubt for many years, but its pilots have come through again and again to keep the airline flying. In the last 15 years, pilots alone have agreed to more than $600 million in tangible concessions in reduced salaries and work rule changes. As a result, TWA pilots today make significantly less, on average, than pilots at other airlines who have equivalent seniority, expertise and training.

Despite those difficulties, ALPA and the pilots it represents have continued to work tirelessly to help TWA achieve success. Due in part to the efforts of TWA's pilots, TWA has achieved consistently high customer satisfaction rankings, on-time performance, and has one of the best safety records in the history of commercial aviation.

The pilots have played an integral role in TWA's future not only as employees, but also as stakeholders and creditors of the airline. Although others may have bankruptcy claims against TWA that contain higher dollar figures, no one has more invested in TWA than its employees—especially its pilots.

ALPA's primary concern regarding the proposed acquisition of TWA by American Airlines is for the long-term stability and professional growth of the 2,300 pilot jobs. However, ALPA believes that, in this specific situation, what is best for the pilots is also in the best interest of the traveling public, the hub state of Missouri, and the jobs, families, lives and communities of our 2,300 pilots and 20,000 TWA employees worldwide.

With all of these interests in mind, ALPA-represented TWA pilots support a complete, fair and sound resolution to this latest and, we believe, final chapter in our airline's history. This resolution will allow TWA and its many constituencies, including its 20,000 employees, to:

- Secure the long-term stability of 20,000 jobs that remain as good or better than they are now.
- Protect the medical and retirement benefits of past TWA employees. Even though ALPA does not represent its retired members in collective bargaining, no one would argue that fulfilling promises to retirees is the right thing to do.
- Avoid ongoing fatal damage from Carl Icahn, who is in no small part responsible for the situation which TWA now finds itself, and who has claimed he is willing to provide economic support to other interested parties.
- Advance a complete, fair and sound resolution, sparing those markets largely served by TWA from economic damage.

For these reasons, we submit that the offer from American Airlines to buy TWA's assets satisfactorily crosses the threshold and meets the criteria outlined above. It is an example of the complete, fair and sound solution we seek. We applaud American for coming forward with this proposal that recognizes the tremendous value of TWA.

In particular, American Airlines Chief Executive Officer Donald Carty has specifically committed in testimony before this Committee "to hire all of TWA's employees and to continue a hub operation in St. Louis." We note especially and favorably Mr. Carty's statement before the Senate Judiciary Committee on February 7 in which he stated, "We look forward to adding TWA's 20,000 employees to the American Airlines family. We are keenly aware of TWA's illustrious history and know that were it not for the hard work and great performance of the people throughout TWA, they would not be the perfect fit for American that we believe they are."

Other bids for TWA's assets are possible, but it is unlikely that any other proposal will be presented that will protect employees, retirees and customers. TWA's financial weakness has been no secret, and during the months when, prior to bankruptcy, TWA management sought buyers, only American came forward.

We respectfully urge the Committee to support the type of complete, fair and sound solution that we seek—a solution that fully addresses the interests of all parties from employees to creditors, consumers and communities; that is fair to all parties and, most important, is sound, ensuring a smooth transition from the TWA of today to a new and more promising future for all concerned.

TRANSPORTATION TRADES DEPARTMENT, AFL–CIO
February 1, 2001

Hon. JOHN MCCAIN,
Chairman,
Committee on Commerce, Science, and Transportation,
Washington, DC.

RE: HEARING ON MERGERS IN THE AVIATION INDUSTRY

Dear Mr. Chairman:

As your Committee reviews mergers in the aviation industry, and specifically the proposed acquisition of Trans World Airlines (TWA) by American Airlines, I write to share with you the views and concerns of the 32 affiliated unions of the Transportation Trades Department, AFL–CIO (TTD).[1] Although we are not directly commenting at this time on the American/TWA issue or the merger of United and US Airways, we are deeply involved in the debate over so-called "airline competition" proposals. We believe Congress must reject proposals that sound good on paper, but fail to consider the effects on service, safety and good jobs.

As amplified in the TTD attached policy resolutions, transportation labor opposes any initiative needlessly threatening the stability of this vital industry and the job security of the several hundred thousand workers employed in the aviation industry.[2] While we understand the concerns expressed by some regarding competition and service, it is patently unfair and contrary to sound transportation policy for the government to favor one segment of the industry over another. For these reasons, TTD and our aviation affiliates opposed the so-called predatory pricing guidelines proposed in 1998 by the U.S. Department of Transportation. Simply put, these regulations did not account for the higher fixed costs of operating a major air carrier and would have made it extremely difficult for these airlines to legitimately defend their market share in a fair business environment against low-cost, typically non-union operators.

Proponents of this policy and other competition proposals justify their plans as necessary to address some of the problems created by the 1978 aviation deregulation. Better than anyone else, we know that deregulation was a risky policy experiment undertaken without any understanding of the impact that it would have on air carriers, service to communities, safety, and workers and their families. While some were touting free-market principles, for working families the result of deregulation was the financial collapse of major pioneer air carriers, including Pan Am and Eastern, and the destruction of tens of thousands of high skill jobs paying good wages and benefits. Over the course of several years following deregulation, bankruptcy rates soared and outsourcing replaced sound investments in facilities and people. It took almost 20 years for the aviation industry to recover from this ill-conceived policy experiment, and that recovery is due in large part to the sacrifices and commitments made by aviation workers.

Some say it is time for our government to intervene in the marketplace and alter the playing field. In our judgement, this would ignore the mistakes made two decades ago by again hastily implementing significant policy changes without considering their effects on the core of the industry and on the men and women who make it the world's finest. Moreover, it would be an injustice for present and past aviation workers to see our government step in on behalf of a special interest segment of

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[1] Attachment 1 is a complete list of TTD's affiliated unions. Specifically, the following aviation unions are members of TTD: the Air Line Pilots Association; the Association of Flight Attendants; the Communication Workers of America; the International Association of Machinists and Aerospace Workers; the International Brotherhood of Teamsters; the National Air Traffic Controllers Association; the Professional Airways Systems Specialists; the Transport Workers Union; and the American Federation of State, County and Municipal Employees.

[2] Attachment 2 are policy resolutions adopted by the TTD Executive Committee in September of 1998 and September of 1999.

the airline industry when our government refused to act on behalf of thousands of workers who were left powerless and with few or no rights during the destructive shake out that followed deregulation.

Aviation employees have done more than anyone to maintain a strong, safe and secure U.S. aviation industry. In seeking to provide more and better air service, we must not sacrifice service, safety and America's working families.

Thank you for your consideration of our views, and I respectfully request that you include this correspondence as part of the official Committee record.

Sincerely,

EDWARD WYTKIND,
Executive Director.

Attachments

cc: The Honorable Ernest F. Hollings, Ranking Member, Committee on Commerce, Science, and Transportation
Members, Committee on Commerce, Science, and Transportation

Attachment 1

TTD Affiliates

The following labor organizations are members of and represented by the TTD:

Air Line Pilots Association
Amalgamated Transit Union
American Federation of State, County and Municipal Employees
American Federation of Teachers
Association of Flight Attendants
American Train Dispatchers Department
Brotherhood of Locomotive Engineers
Brotherhood of Maintenance of Way Employes
Brotherhood of Railroad Signalmen
Communications Workers of America
Hotel Employees and Restaurant Employees Union
International Association of Fire Fighters
International Association of Machinists and Aerospace Workers
International Brotherhood of Boilermakers, Blacksmiths, Forgers and Helpers
International Brotherhood of Electrical Workers
International Brotherhood of Teamsters
International Longshoremen's Association
International Longshoremen's and Warehousemen's Union
International Organization of Masters, Mates & Pilots, ILA
International Union of Operating Engineers
Marine Engineers Beneficial Association
National Air Traffic Controllers Association
National Association of Letter Carriers
National Federation of Public and Private Employees
Professional Airways Systems Specialists
Retail, Wholesale and Department Store Union
Service Employees International Union
Sheet Metal Workers International Association
*Transportation * Communications International Union*
Transport Workers Union of America
United Mine Workers of America
United Steelworkers of America

January 2001

Attachment 2

Resolution No. 1

Protecting Workers From Airline "Competition" Proposals

In recent months a number of dangerous and counterproductive proposals have surfaced including the Administration's policy on unfair exclusionary conduct and TTD-opposed slot confiscation programs designed to promote competition in the airline industry. While transportation labor supports the concept of providing consumers and businesses with fair and competitive air transportation, this goal cannot be achieved at the expense of workers who just now are emerging from a difficult 20-year period since deregulation.

When the airline industry was deregulated in 1978, few protections were offered to long-time workers and in fact no group has suffered more in this volatile environment than airline employees. These consequences were predicted by airline unions and that is why they opposed this dangerous policy experiment. Major carriers have gone bankrupt and over 100 smaller carriers have faced the same fate. Industry pioneers and giants such as Eastern, Pan American and Braniff were liquidated as their employees saw their careers and years of service evaporate in the name of the free market. In fact, in the late 1980s and early 1990s the major carriers experienced billions of dollars in financial losses that threatened the viability of this industry and the security of tens of thousands of jobs. Workers were simply told that the unemployment, job dislocation, pressure on wages and benefits and the loss of collective bargaining rights that followed deregulation were natural consequences of a freer marketplace and that government could not interfere.

Many carriers were able to survive deregulation only by working with their unionized employees to restructure the workplace, alter wages and benefits, and reform work rules and procedures. In 1993 Northwest Airlines, on the brink of financial collapse, turned to its workers whose cooperation allowed management to restructure debt and avoid certain and potentially disastrous bankruptcy proceedings. In 1994 pilots, mechanics and fleet service employees at United Airlines became part owners by exchanging a 55 percent stake in the company for almost $5 billion worth of concessions. At TWA, employees have worked with management and restructured their contracts more than once to help this ailing carrier survive continuing financial turbulence.

Airline employees who retained their jobs during deregulation became partners with and investors in their companies. Now these investments are starting to pay off as airline corporations are once again flying high with record revenues and profits. Unfortunately some want to ignore recent history and alter the playing field with little regard for what the changes mean for workers whose sacrifices allowed this industry to become the economic success that it is today.

This point has been raised time and time again by unions that have voiced their opposition to the Administration's proposed policy regarding unfair exclusionary conduct—so called predatory pricing guidelines. These guidelines inappropriately favor one segment of the industry—new entrant carriers—at the expense of established airlines and their workers. By restricting the ability of major carriers to aggressively respond to low-fare salvos into the marketplace, the guidelines would favor new entrant carriers whose low fares are achieved by paying substandard wages and benefits and outsourcing safety-sensitive aircraft maintenance functions. Our government should not respond by rewarding these carriers with a policy-imposed competitive advantage.

To compensate for their higher fixed costs, which include good wages and benefits that support working families, established carriers have complicated fare structures. In order to compete effectively, these fares need to be flexible and are subject to change. Instead of recognizing this competitive reality and the fact that these carriers support the highest safety and worker compensation standards, the guidelines punish major carriers who defend their routes and market share. Meanwhile new entrant carriers are left free to use their lower wage scale to compete in a market place that is artificially protected by a government policy that actually deters vigorous competition.

Contrary to what some have argued, transportation labor's position on this issue is not based on a simple desire to protect carriers that employ our members. The reality is that most new entrants will eventually become unionized and in fact at a number of smaller carriers employees have already chosen to enjoy the benefits that union representation and collective bargaining can bring. TTD's position is driven by our unique perspective on deregulation in general and our specific experience in aviation. We have seen what effects ill-advised government policies can have on our industry not only for workers, but for communities and businesses that depend on air service. The promotion of competition cannot be attained by favoring one sector of the industry over the other with worker interests once again left hanging in the balance.

THEREFORE, BE IT RESOLVED:

- That TTD will voice its formal opposition to the Department of Transportation's proposed policy statement regarding unfair exclusionary practices; and

- That TTD will work with interested affiliates to educate policy makers about the impact the 1978 decision to deregulate the industry had on the aviation workforce and the impact that subsequent government action would have on these same employees.

Resolution No. 1–98 (s)
(Adopted September 23, 1998)

Resolution No. 1

The Administration and Congress Should Scrap Harmful "Airline Competition" Proposals

With major aviation legislation pending in Congress, calls are once again being heard for the imposition of airline competition proposals that would repeat the mistakes associated with airline deregulation by ignoring the severe effects on employees. Transportation labor is firmly on record opposing these proposals, including the U.S. Department of Transportation's (DOT) draft enforcement policy on unfair exclusionary conduct, for the simple reason that these measures would unfairly disadvantage established major carriers and their workers as they attempt to compete with air carriers that provide employees with substandard wages and benefits. (See Resolution No. 1–98.)

At the Transportation Trades Department, AFL–CIO's (TTD) fall 1998 meeting, the Executive Committee described these policy proposals as "dangerous and counterproductive" and said that "by restricting the ability of major carriers to aggressively respond to low-fare salvos into the marketplace, the guidelines would favor new entrant carriers whose low fares are achieved by paying substandard wages and benefits and outsourcing safety-sensitive aircraft maintenance functions." The Executive Committee also pointed out that many of today's air carriers such as Northwest survived the brutal shake-out inspired by airline deregulation ". . . only by working with their unionized employees to restructure the workplace, alter wages and benefits, and reform work rules and procedures."

Transportation labor reaffirms its opposition to competition measures that threaten the livelihood and job security of aviation workers who have contributed so much to the industry's remarkable economic turnaround. Whether couched in terms of slot confiscation plans, unexplained pricing guidelines, or other initiatives that unfairly favor one segment of the industry over the other, the result is the same—a stranglehold would be placed on established carriers faced with the dumping of new air service by start ups. While monitoring the conduct of corporations is an important government function, the economic rights of existing companies and their workers to compete and operate in the complex world of air travel cannot be ignored.

Congress agreed with many of these concerns and last year acted to bar the Administration from implementing the guidelines until the DOT and the independent Transportation Research Board (TRB) conducted separate studies on airline deregulation. While flawed in many respects, including its endorsement of changing foreign ownership restrictions, the recently released TRB report concluded that the Administration's guidelines could inhibit genuine competition and that certain carriers would receive special treatment. Specifically, the report declares that ". . . distinguishing between legitimate and questionable competitiveness responses poses significant challenges, and raises the possibility of false charges of predation . . . ."

Although the effects of flawed competition measures on aviation employees were ignored by the TRB, its warning against the Administration's competition guidelines underscores the serious problems posed by government intervention that fails to recognize the legitimate rights of established air carriers to compete in a far more liberalized marketplace. Transportation labor calls on the Clinton Administration and Congress to heed the TRB's warning and refrain from pursuing any competition measures whose consequences could be severe for major U.S. air carriers and their employees.

THEREFORE, BE IT RESOLVED:

- That TTD reaffirms its opposition to ill-advised airline competition measures that disadvantage major air carriers and their workers in favor of start-up airlines;
- That TTD educates Congress on the threats posed by federal government intervention favoring start-up carriers that maybe incapable of assuring the same level of service, efficiency and safety as established air carriers; and

- That TTD and its Aviation Coordinating Committee aggressively opposes any attempts by the Clinton Administration or Congress to advance competition policy proposals that again fail to protect the jobs and rights of aviation workers.

Resolution No. 1–99 (F)
(Adopted September 29, 1999)

PREPARED STATEMENT OF LEONARD L. GRIGGS, JR., DIRECTOR OF AIRPORTS—CITY OF ST. LOUIS, MO

Mr. Chairman and Members of the Committee: I am Leonard L. Griggs, Jr., Director of Airports for the City of St. Louis. The City is the owner and operator of the Lambert-St. Louis International Airport, historically the main hub for TWA. Thank you for allowing me the opportunity to submit the views of the City of St. Louis regarding the proposed acquisition of TWA assets by American Airlines.

Mr. Chairman, not all mergers are created equal. As Senator Carnahan recently stated before this Committee, "While we may be initially inclined to view all of the current airline mergers in the same light, we must consider the American Airlines' acquisition of TWA independently of the other proposed mergers." The City of St. Louis agrees.

American/TWA Merger is not Like Other Mergers

The American-TWA proposed agreement is unlike any other mergers currently being discussed. Contrary to press reports, and the opinion of many pundits and even some critics in Congress, the proposed acquisition will not necessarily harm the development of the airline industry or be anticompetitive for consumers. On the contrary, given TWA's current financial condition, I believe that consumers would be worse off with the possible alternatives had American Airlines not come forward with its proposal to acquire TWA. This is why St. Louis fully supports the proposed transaction.

It was recently stated in our local newspaper that "TWA, after years of valiantly trying to turn around, is out of time and out of money." In contrast to its previous financial problems, this time it seems clear that without outside help TWA would have been forced to stop flying and simply liquidate its assets. American Airlines came forward with its proposal in the very same week that TWA would have stopped operating due to lack of funds. Reportedly, Mike Palumbo, TWA's CFO, testified before a Delaware bankruptcy court judge last week that, without American's debtor-in-possession financing, TWA would have ceased to operate. Instead, American's commitment of $200 million in debtor-in-possession financing has allowed TWA to continue serving the public until the transaction is completed.

In short, Mr. Chairman, without the American deal, TWA would have ceased to compete in the marketplace. However, this acquisition should not raise concerns of reducing or stifling competition. Instead, it is my opinion that the proposed deal is simply making the best of a worrisome situation.

Over the last few weeks, it became abundantly clear to us that TWA's options were fast disappearing. Since TWA no longer had the possibility of maintaining healthy, financially robust operations to compete with the other U.S. regional or network carriers, we were left with the choice of allowing American to take TWA as a whole, or allowing TWA to fail, and let others pick at the carcass.

TWA is "Failing Airline" in Merger Parlance

This is a classic example of a failing airline whose on-going business concern can only be rescued by allowing it to merge with a healthy airline. Indeed, although federal policy does disfavor the acquisition of healthy air carriers by their competitors, there is a long-standing exception when the proposed acquisition involves a failing carrier. The rationale for the exception is that, no matter what, a failing airline will not remain in the market. I believe that, by now, there is enough evidence to conclude that TWA will simply cease to exist. Therefore, the key question that must be answered is how to maximize the public benefit in the distribution of its assets.

Bill Compton, TWA's CEO, was quoted as saying that he has been "shopping" the airline for some time, and has had no other viable offers for its acquisition as a going concern that would preserve its name and intangible assets. Moreover, although it is true that certain assets (such as slots and leased aircraft) could be sold and placed into service absent the proposed transaction with American Airlines, most of TWA's many valuable assets and resources (such as certain gatehold rights at Lambert, St. Louis aircraft maintenance facilities, and, more importantly, TWA's St. Louis workforce) would have been underused.

For St. Louis, the choice is clear. If the proposed acquisition is not allowed to proceed, St. Louis risks losing its air carrier hub. Without a large airline hubbing at our airport, our community will lose large numbers of well-paying jobs, as well as its close link to national and international markets that makes our region a favored business location.

Air Service Requirements of St. Louis Area Are Substantial

Without TWA's operations, St. Louis risks the loss of substantial levels of air service. Although TWA is only one of nine major airlines serving the airport, it alone provides 73 percent of the daily flight departures from the airport. TWA's 374 daily flights out of St. Louis serve more than 100 non-stop markets, 65 of which would not otherwise receive non-stop service. Without the TWA-American agreements St. Louis would lose valuable air service to many communities throughout the United States, and possibly, the world. So far, other than American Airline's proposal, no other credible plan has been offered in the bankruptcy process which would maintain St. Louis' present level of air service.

New St. Louis Runway Capacity Supported by American Airlines

American Airlines' promise to serve St. Louis means the continuing use of the City's public airport infrastructure. In fact, American Airlines has stated that, after it completes its acquisition of TWA assets, it intends to use the St. Louis airport and TWA's gates for a mid-continental hub.

And, Mr. Chairman, in connection with American's commitment to the St. Louis community, I have been assured by American's senior management, following an extensive briefing on our new runway project, that American will be fully and enthusiastically supporting our new runway (W–1W) expansion plan. This early decision by American is critical to keeping our expansion on schedule so that Lambert can maintain its hub status and remain competitive.

Local TWA Employment Would be Protected

The risk of mass unemployment in our area is real. If TWA were to shut down, it could leave 20,000 TWA employees out of work, including almost 9,000 in our immediate area, and 12,000 throughout Missouri. TWA is the second largest employer in the City of St. Louis, and the seventh largest in the metropolitan region. It has been estimated that TWA's operations in St. Louis contribute approximately $5 billion annually to the local economy. American Airlines has proposed to maintain TWA's unionized workforce and as much of its administrative employees as feasible.

Conclusion

Mr. Chairman, I ask that you consider American Airlines' proposal to acquire TWA assets not as a competition-reducing merger. If TWA were to shut down and liquidate, the City of St. Louis would lose most of its air service, close to 9,000 of its area citizens could be forced to stand in the unemployment line, large amounts of existing valuable airport infrastructure would go unused, and valuable new national runway capacity might go undeveloped. We cannot let that happen. That is why St. Louis fully supports the proposed acquisition of TWA.

Thank you.

PREPARED STATEMENT OF RICHARD BIDWELL,
ST. LOUIS CONVENTION AND VISITORS COMMISSION

- Maintaining hub status in St. Louis is critical to the community's continued growth as a convention, meeting and tourism destination.
- American Airlines provides a hub in St. Louis and the potential for additional future growth.
- The high number of arrivals and departures from Lambert-St. Louis International Airport is critical for meetings, conventions and leisure visitors coming to St. Louis.
- American Airlines has an excellent reputation among meeting, convention and incentive travel planners. The airline has an aggressive position toward marketing itself to those important groups.
- An American Airlines hub in St. Louis provides the St. Louis Convention & Visitors Commission with new opportunities for partnerships with other AA gateways to encourage travel to St. Louis.
- The strong American system gives international travelers greater opportunities to visit St. Louis. This is especially critical because St. Louis will be hosting the

Travel Industry Association of America's International Pow Wow travel trade show in May 2003. This event brings travel buyers from across the globe to St. Louis to meet with travel industry suppliers.

- American Airlines has an excellent reputation as a good corporate citizen. This is critical to the quality of life in St. Louis.
- The future of TWA has been an issue with convention and meeting planners considering St. Louis for their groups several years out. However, since the announcement of American's offer to purchase TWA's assets and maintain a hub in St. Louis, groups such as Dallas-based Price, Waterhouse, Coopers which had been considering Chicago, Dallas and other cities for their meeting—now are considering St. Louis.
- American's establishment of a St. Louis hub will help us change perception of St. Louis in major markets like Chicago.
- American's frequent flyer program is better, with more subscribers than TWA's program.

ST LOUIS REGIONAL CHAMBER AND GROWTH ASSOCIATION

January 31, 2001

Mr. JOHN M. NANNES, Esq.
Acting Assistant Attorney General,
Antitrust Division,
United States Department of Justice,
Washington, DC.

RE: AMERICAN AIRLINES ACQUISITION OF TWA IS VITALLY NECESSARY FOR ECONOMIC SURVIVAL OF ST. LOUIS METROPOLITAN AREA

Dear Mr. Nannes:

I write to you on behalf of the St. Louis Regional Chamber and Growth Association ("RCGA"), to voice our whole-hearted support for American Airlines' proposal to buy TWA outright and incorporate its operations, facilities, equipment, and employees into American.

RCGA is the regional chamber of commerce for those areas of Missouri and Illinois that fall within the St. Louis metropolitan area. It is the only regional economic development organization working for economic growth and improved quality of life throughout the twelve-county region. It is a civic, not-for-profit association. RCGA has more than 4,000 members, including representatives of labor, large and small businesses, and professional organizations. RCGA has long supported the development and expansion of airport capacity and air service, because it recognizes that the future economic development of the St. Louis region is inextricably intertwined with enhanced airport capacity.

By supporting this transaction, we do not favor the particular interest of American or TWA, but rather seek to protect the continuing vitality of the region's enormous investment in Lambert, and the interest in securing and furthering regional economic development, which demands a continued hub airline presence at Lambert.

Lambert has been serving the St. Louis region since before 1920, just a few years after the Wright Brothers' pioneering flight. At approximately 2,100 acres, Lambert is one of the smallest major airports in the United States, Despite its constrained size, Lambert International Airport is extraordinarily busy. In 1999, Lambert ranked 11th nationally in total aircraft operations. In 1999, approximately 15.1 million passengers boarded aircraft at Lambert, 180 percent increase from the 5.4 million who did so in 1980. The projected number for the year 2015 is 20.9 million.

Billions of dollars in public and private funds have been invested to develop Lambert and its immediate environs in its current configuration. The fabric of regional economic activity has woven itself around this critical community asset. Countless investments and business relationships depend on it. To name but a few:

- The region's surface transportation infrastructure is designed to bring passengers and others to and from Lambert. Interstate highways I–70, I–170, and I–270 were all routed to facilitate airport access. The Metro-Link light rail transit line, with two stations at Lambert, terminates at the airport.
- Airport-related businesses, such as in-terminal businesses, hotels, automobile rental agencies, and frequent air shippers, have sunk major investments into their existing locations.

- Residential and business location patterns have developed concurrently with the airport. Due in part to airport-related economic activity, the industrial, residential, and office development in the St. Louis region area are now centered on this Lambert environs. Lambert is today very close to the residential population center of the St. Louis region.
- Many steps have been taken over the years to make building heights, noise-sensitive uses, and sound insulation in the areas near Lambert compatible with its continued operation.

Lambert currently operates under severe constraints in bad weather due to its runway configuration. The City of St. Louis, the FAA, airport staff, and many others have spent the last several years preparing for a major airport expansion. Now that the legal challenges to expansion are over, and the expansion program is underway, it would be a waste of precious aviation capacity not to use the expanded airfield to its fullest potential. American's proposed acquisition of TWA would take full advantage of the airport expansion.

The Lambert air service hub benefits the economic health of the region in two ways. First, the hubbing operation itself creates jobs directly and indirectly. TWA's use of Lambert as its primary mid-continent hub brings major economic benefits to the region; only adoption of Lambert as the major hub of another airline will continue those benefits. It has been estimated that Lambert contributes some $5.1 billion to the region's economy today, including some 16,800 directly or closely-related airport jobs. If Lambert can continue as a viable hub, the number of directly or closely-related jobs is expected to double by 2015; annual economic impact of an expanded Lambert is projected to more than double to the $12 billion to $15 billion level. This rate of growth far exceeds the 11 percent growth projected for all metropolitan area jobs.

Second, the presence of the hub provides the region with excellent air service, which entices businesses to locate and expand in the region. Loss of the hub could mean loss of jobs and great inconvenience to the traveling public.

Enlarged economic activity and strong air travel connections both enhance the role of the St. Louis region in the national and global economy.

In conclusion, we recognize that any acquisition of a major air carrier raises concerns about the resulting competitive landscape that will face consumers. But TWA is not a candidate for independent survival in the long run. American's proposed acquisition of TWA has the potential to preserve (and, in fact, enhance) the economic vitality of the St. Louis airport hub and the surrounding region. In comparison, if the proposed acquisition is not allowed to proceed, we believe that St. Louis would lose its air carrier hub, would lose substantial numbers of well-paying air carrier jobs, and would lose the close link to national and international markets that makes it a favored business location.

We believe that the proposed acquisition is absolutely necessary for the economic survival of our region. We urge you to support it.

Sincerely,

RICHARD C.D. FLEMING,
President and CEO.

AMERICAN SOCIETY OF TRAVEL AGENTS
February 7, 2001

Hon. JOHN MCCAIN,
Chairman,
Senate Commerce Committee,
Washington, DC.

Dear Mr. Chairman:

The American Society of Travel Agents (ASTA) applauds your efforts to monitor competition in the aviation industry by conducting the February 1, 2001 hearing on "Airline Acquisition." As a proponent of airline deregulation and an advocate of the traveling consumer, ASTA is deeply concerned about the excessive concentration within the airline industry.

With the looming American Airlines acquisition of Trans World Airlines' assets, the proposed merger of United Airlines and U.S. Airways, along with the potential for further mergers among Delta Airlines, Continental Airlines and Northwest Airlines, the Nation will be left with no more than three giant carriers. The result is an unregulated shared monopoly in which consumers face increasing prices, fewer choices and further deterioration in already unacceptable service.

Attached is an editorial that was featured in the *New York Daily News,* on Sunday, January 21, 2001, entitled, *Mergers: The latest air rage.* This editorial represents the views and concerns of ASTA, and we ask that it be included in the hearing record.

Sincerely,

RICHARD M. COPLAND, CTC,
President and CEO.

Attachment

Mergers: The latest air rage

By Richard M. Copland

If the U.S. Department of Justice approves the two deals pending between United Airlines/US Airways and American Airlines/Trans World Airlines, it will be the deathblow to competition in the airline industry.

And that would be a disaster for customers. Simply put, reduced competition means higher prices, less service and serious disruptions in travel when, inevitably, there's a labor dispute.

Without price and route competition, the traveling public would be held hostage by a few monster airlines. It would mean less aggressive discounting by the airlines, less willingness to challenge one another in new markets and more follow-the-leader behavior.

According to Merrill Lynch, if the American/TWA and the United/US Airways deals are allowed to proceed, United will control 26 percent of the domestic market, while American will control 25 percent. That sounds bad, but it doesn't tell the whole story.

These giant airlines already have divided up the country and agreed not to compete on many routes. At Kennedy Airport, where American already controls 27 percent, the merger with TWA would increase American's share to 48 percent. That means if you fly out of JFK domestically, chances are you'll pay more than ever.

In "Competition in the U.S. Domestic Airline Industry," the U.S. Department of Transportation said, "High fares in shorter-distance markets come about at hub airports where one major network airline has a dominant market share. Average fares at some of the airports can be 50 percent to 60 percent higher when compared to more competitive markets." Just ask the folks in upstate Rochester, where the price for a one-way ticket to Chicago, for instance, is $789. But the price for a ticket from Salt Lake City to Spokane, Wash., a route that's roughly the same distance but is serviced by a low-fare carrier (Southwest), is $393.59.

With the approval of these huge deals, competition in markets throughout the country would be eliminated. American and United would share in an agreed division of time slots on the heavily traveled East Coast shuttles. United/US Airways' merger would establish dominance in Washington for United by controlling about 60 percent of domestic seats and eliminating competition to 30 cities. American/TWA would give American a market share in San Juan of 59 percent. And on and on.

But it's not just about fares. It's also about service. Travel should be a profitable pleasure—profitable for the airlines and a pleasure for the consumers. As the major carriers consolidate, the record of declining customer service has become a national disgrace.

In the first half of 2000, consumer complaints to the U.S. Transportation Department rose 69 percent over the previous year. According to Inspector General Kenneth Mead, one in five flights arrived late in 1999, with delays averaging about 50 minutes. The number of flights with taxi-out times of one hour or more increased 130 percent in the past five years.

Travel agents sell about 80 percent of airline tickets. We listen to our customers' frustrations about airline service daily, and we intend to do something about it.

The American Society of Travel Agents strongly believes that no more mergers, buyouts or airline alliances should be allowed until an Air Travelers' Bill of Rights is approved by Congress. Our organization proposed such a bill two years ago, and the airlines scoffed at it. They still do.

If every plane is full and profits are fat, but passengers are fuming, what kind of a national transportation system do we have?

Labor issues are another major consumer concern. We survived the last American shutdown, but it was touch-and-go. With just two or three supergiants, how would the country fare in an extended labor dispute? It could have disastrous economic consequences for our country's economy.

The government must act now to protect consumers. A concentration of a handful of supergiant airlines means it would be far easier for price hikes to stick and airlines to ignore the needs of the traveling public, the rightful owners of the airways.

If airlines want to increase market share, they should have to earn it by winning the loyalty of the customer, not by gobbling up competitors.

Copland is president and CEO of the American Society of Travel Agents.

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