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BEFORE THE

DEPARTMENT OF TRANSPORTATION

WASHINGTON, D.C.

DEPT. OF TRANSPORTATION  
OFFICE

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Joint Application of

AMERICAN AIRLINES, INC. and  
LINEA AEREA NACIONAL CHILE, S.A. (LAN CHILE)

Docket OST-97-3285-52

under 49 U.S.C. Sections 41308 and 41309 for approval  
of antitrust immunity for alliance agreement

OBJECTIONS OF  
CONTINENTAL AIRLINES, INC.

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OBJECTIONS OF  
CONTINENTAL AIRLINES, INC.

The tentative decision to approve the alliance between American<sup>1</sup> and Lan  
Chile rests on demonstrably erroneous assumptions:

- The tentative decision assumes that the “economic efficiency and further competition” generated by alliances such as Northwest/KLM will produce comparable public benefits in the Southern Cone<sup>2</sup> of South America under vastly different circumstances, but the dominance of American and its allies, Lan Chile and Aerolineas Argentinas, in the Southern Cone will actually reduce competition and increase fares.

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<sup>1</sup> Common names of carrier are used.

<sup>2</sup> The Southern Cone is that area of South America comprising the countries of Argentina, Chile, Paraguay and Uruguay.

- Although the tentative decision says “the U.S.-Chile open-skies accord will foster new entry and enhanced competition in the U.S.-Chile aviation markets,” the more likely result, especially with an immunized American/Lan Chile alliance, will be reduced service and less competition because U.S. airlines will not be able to “take advantage of those [new] opportunities” due to the dominance of American and its allies on the thin U.S.-Chile routes, which are very different from U.S.-Central America and U.S.-Europe routes.
- Instead of introducing multiple global networks onto the U.S.-Southern Cone routes, granting antitrust immunity to American/Lan Chile will support American’s effort to drive other competitors out and block the entry of competing global networks in the Southern Cone.
- The Department says the “enhanced service options” of the American/Lan Chile alliance cannot be achieved without antitrust immunity, but antitrust immunity is not needed to achieve those options and the alliance should be disapproved.
- The Department assumes the anticompetitive harm of an antitrust-immunized American/Lan Chile alliance can be ameliorated by less stringent conditions than the Department has imposed on other alliances, but more stringent conditions are required to alleviate the serious anticompetitive harm produced by combining American and Lan Chile.

For the following reasons, Continental objects strongly to the tentative decision to approve the American/Lan Chile alliance and grant antitrust immunity for it.

I. THE AMERICAN/LAN CHILE ALLIANCE IS MORE ANTI-COMPETITIVE THAN EVER, AND IT SHOULD BE DISAPPROVED

A. An Immunized American/Lan Chile Alliance Will Perpetuate De Facto Closed U.S.-Chile Skies

The Department's erroneous conclusion that it is "unlikely that the Alliance Agreement . . . will substantially reduce competition in any relevant market" (Order 99-4-17 at 13) appears to be based on the Department's failure to realize just how anticompetitive the American/Lan Chile alliance would be. An antitrust-immunized alliance between American and Lan Chile is a critical component of American's global effort to drive out competitors and pre-empt pro-competitive alliances since it would allow American to manipulate open skies in Chile and closed skies in Argentina<sup>3</sup> to align American with the two major carriers headquartered in the Southern Cone, expand American's command of U.S.-South America traffic and construct an impenetrable network of service throughout the Southern Cone. Approval of the American/Lan Chile alliance with antitrust immunity would enable American and Lan Chile, the two dominant U.S.-Chile nonstop carriers, effectively to control U.S.-Chile skies, de facto closing the skies by preventing other U.S. carriers from competing effectively in these de jure "open" skies. With the Argentine skies closed to new entry, some 20% of the U.S.-Buenos

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<sup>3</sup> Just yesterday the possibility of the U.S. and Argentina reaching an open-skies agreement grew even more remote when Argentina postponed aviation talks with the U.S. indefinitely. See Aviation Daily, May 20, 1999, at 1 (Electronic Edition).

Aires traffic moves over other points because U.S.-Argentina capacity is insufficient to meet demand, and American's immunized alliance with Lan Chile will allow the immunized partners to control U.S.-Santiago-Buenos Aires flights, one of the most logical routings for Buenos Aires service, while American and Aerolineas Argentinas block direct new entry into Argentina. American's attempt to establish a Southern Cone monopoly by its partial acquisition and effective control of Aerolineas Argentinas already has seriously exacerbated the competitive dominance American amassed in the Southern Cone and throughout South America. American has signed up alliance partners throughout Latin America, pre-empting more competitive alliances, with the clear objective of co-opting foreign carriers in American's drive to eliminate competitors.

Would-be monopolist American will be the winning bidder for a Lan Chile alliance if the Department's tentative decision is confirmed, but the Department should not rap the auctioneer's gavel. The "sound commercial criteria" and "free, competitive process" envisioned by the Department has been subverted by the commercial fact that American and Lan Chile joined together will be able to achieve monopoly power to maximize their own profits to the detriment of the public interest and competition. The American/Lan Chile combination is the result of American's successful plan to lure Lan Chile into an alliance based solely on maximizing profits to both companies through the elimination of competition.

American today operates 60% of the U.S. carrier nonstop flights between the U.S. and Chile.<sup>4</sup> American is the only U.S.-flag carrier with a two-hub U.S.-Chile route system. American's chief competitor on U.S.-Chile routes is Lan Chile, which operates 100% of the Chilean-carrier nonstop flights. Together, American and Lan Chile operate 69% of nonstop U.S.-Chile flights, while United and Continental operate only one daily nonstop each.

The Department's tentative decision to allow already-dominant American to join forces with its chief U.S.-Chile competitor would give American/Lan Chile so much control of U.S.-Chile routes that no other carrier would be able to catch up. American, having been driven off of "open skies" routes by antitrust-immunized alliances itself (see Written Testimony of Robert L. Crandall, then-Chairman and Chief Executive Officer, AMR Corporation, before the Senate Judiciary Subcommittee on Antitrust, March 19, 1998, at 2, 8), knows how to drive out the competition. And American doubtless intends to do so. Miami is the predominant gateway to Chile, just as it is the key U.S. gateway for the rest of Latin America. The combined strength of American and Lan Chile, particularly in light of their dominance of Miami-Santiago routes, coupled with the pre-emptive agreements American has struck with other carriers throughout Latin America, would substitute commercial barriers for the existing bilateral barriers to entry, and no

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<sup>4</sup> April 1999 OAG.

U.S. or foreign carrier would be able to mount an effective competitive assault on the American/Lan Chile dominance over U.S.-Chile routes.

Moreover, the American/Lan Chile/Aerolineas Argentinas alliance would control together 65% of nonstop flights between the U.S. and the Southern Cone. American operates 50% of U.S.-carrier nonstop U.S.-Argentina flights, and Aerolineas Argentinas operates 100% of Argentinean-carrier nonstop U.S.-Argentina flights. Together, American and Aerolineas Argentinas operate 62% of nonstop U.S.-Argentina flights. Unless the Department reverses its tentative approval of the American/Lan Chile alliance, American and its Southern Cone partners will be able to respond quickly, mightily and effectively to stop competitive efforts by new entrants challenging their domination in the region.

The Department assumes erroneously that more U.S.-Chile nonstop service will naturally flow from the U.S.-Chile open-skies agreement. On the contrary, American's dominance of U.S.-Chile nonstop flights with Lan Chile may result in fewer flights by other carriers. The only unfulfilled proposals for additional Chile service are one-stop flights by Delta and United via Sao Paulo, and United has already been forced to abandon its Lima-Santiago service and its second daily Miami-Santiago service which was operated over Lima. Although highly-circuitous service via Sao Paulo may drain some connecting traffic from Continental's service, more direct service by American and Lan Chile via Miami, Dallas/Fort Worth and New York will assure that any Sao Paulo service remains marginal at best.

American and Lan Chile have 31 weekly frequencies between the U.S. and Chile, more than double the combined total of other carriers. (See April 1999 OAG) The American/Lan Chile control of U.S.-Chile skies will inevitably result in fewer competitive challenges than if American and Lan Chile were independent competitors under de facto and de jure open-skies conditions.

Eliminating competition would serve American's and Lan Chile's private commercial interests, but clearly it would not serve the public interest. The Department's statutory mandate to "disapprove" an agreement that "substantially reduces or eliminates competition" and is not "necessary to meet a serious transportation need or to achieve important public benefits"<sup>5</sup> and the public interest<sup>6</sup> compel the Department to reverse its tentative decision and disapprove the American/Lan Chile alliance. The Department's approval of the American/Lan Chile alliance would damage competition irrevocably, allowing American and Lan Chile to dominate nonstop U.S.-Chile passenger traffic more than they do today and enabling American and its Southern Cone partners to foreclose the possibility of effective global network competition in that area of South America.

If the Department does not reverse its tentative decision, the few remaining unaligned Latin American carriers will become convinced that the Department is

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<sup>5</sup> 49 U.S.C. 41309(b)(1)(A), (B).

<sup>6</sup> The Department can grant code-share applications only if it finds they are in the public interest. See 14 C.F.R. § 207.10(g).

unwilling to curb American's anticompetitive strategy in Latin America and, thus, that they must join the expanding American network of Latin American alliances and maximize their profits by joining a would-be monopolist or risk commercial annihilation.

B. The Experience Of U.S.-Europe And U.S.-Central America Alliances Does Not Provide An Accurate Barometer For The Results Of An Immunized American/Lan Chile Alliance

The Department's reliance on experiences with alliances in Europe and Central America to predict favorable results from immunizing American/Lan Chile is misplaced. Although American itself says it has been driven off of European "open-skies" routes by antitrust-immunized alliances, conditions in South America will enable American/Lan Chile to drive competition out far more easily than any European alliances could hope to do. Although Europe is characterized by numerous hubs competing for connecting traffic throughout Europe, Santiago and Buenos Aires are spokes, not hubs, and there are no feasible alternatives for connecting traffic served via either point. The geographic difference is crucial, since competition among carriers providing nonstop and connecting services and among major hubs is strong in Europe and non-existent in the Southern Cone. American and its Southern Cone partners will control the spoke traffic and dominate the only two Southern Cone connecting points and the primary O&D points: Santiago and Buenos Aires. The Department cites the Northwest/KLM alliance as a precedent for the American/Lan Chile alliance, but the two alliances are very different. The Northwest/KLM alliance has only a small percentage of U.S.-Europe traffic and

numerous major hubs compete with Amsterdam. American and its Southern Cone partners have the majority of U.S.-Southern Cone traffic, they control the thin spoke traffic and their hubs face no competition for the limited amount of connecting traffic.

Similarly, experience in Central America is no precursor of likely results in the Southern Cone. Central America is fundamentally different for several reasons. Unlike operations between the U.S. and the Southern Cone, flights between the U.S. and Central America use smaller aircraft and are much shorter in distance, requiring less aircraft time and allowing airlines to use their fleets for U.S. and Central America flights in the same day. Thus, carriers can institute spoke service in Central America much as they would within the U.S. Airlines operating nonstop service between the U.S. and the Southern Cone must operate larger aircraft, fly their aircraft long distances and leave the aircraft idle for an entire day in South America to compete in the prime time channels for the limited spoke traffic available. By contrast, American and its partners will be able to operate aircraft more efficiently, use their aircraft during the day on Southern Cone routes, dominate the connecting points and drive out competitors.

II. ANTITRUST IMMUNITY IS NOT REQUIRED TO ACHIEVE THE "ENHANCED SERVICE OPTIONS" CLAIMED BY THE AMERICAN/LAN CHILE ALLIANCE, AND THE ALLIANCE SHOULD BE DISAPPROVED

The tentative decision cites "enhanced service options" as a benefit of immunity, but antitrust immunity is not required to achieve any enhanced service options resulting from an American/Lan Chile alliance. "New online service" can be

established through code-sharing without antitrust immunity, and American has failed to demonstrate how "operational efficiencies" will benefit the public.

Continental does not question that the aligned American/Lan Chile will be able "to operate more efficiently" by coordinating "all of their U.S.-South America business activities, including scheduling, route planning, pricing, marketing, sales and inventory control." (Order 99-4-17 at 13, 22) The question before the Department is whether it wants to make would-be monopolists "more efficient" at exploiting their dominance. If American and Lan Chile are denied antitrust immunity, the net result might be more service options for the public since American and Lan Chile would be unable to coordinate reductions in service and eliminate fare and service competition between them. With antitrust immunity, American and Lan Chile clearly "will be ending their competitive service in some markets . . .", resulting in a negative impact on the public. (Order 99-4-17 at 22)

The Department's tentative decision cannot justifiably conclude that additional cooperative activities made possible through antitrust immunity, when taken alone, would yield substantial public benefits outweighing the clear anticompetitive harm of granting antitrust immunity. Since there are no such benefits, the Department's tentative decision to grant antitrust immunity is unjustified.

Without antitrust immunity or a Lan Chile alliance, American today can serve all of the behind U.S.-gateway points on its route system, and the beyond-

Santiago points covered by the American/Lan Chile proposal produce little traffic. The Department's tentative decision to allow the two dominant U.S.-Chile carriers to agree on capacity reduction will create harm, not public benefit, because it will permit American and Lan Chile to manipulate their capacity against competitors. American does not need antitrust immunity or Lan Chile to expand globally or on U.S.-Latin America routes. If American and Lan Chile are not allowed to pursue their anticompetitive alliance, Lan Chile could form an alliance with Continental, United, Delta or any other U.S. carrier to gain increased U.S. access.<sup>7</sup> Unlike an American/Lan Chile alliance, a Lan Chile alliance with Continental or another carrier would expand options for passengers and shippers by providing multiple competing service options and alternatives to the existing American network.

There are no antitrust-immunized alliances involving U.S. and Central American carriers to block the benefits of competition. If the Department believes Central America is a model for airline competition, the Department should conclude that, for Chile, as for Central America, antitrust immunity is not required to promote market entry and to create more service options and benefits to the public.

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<sup>7</sup> Although Lan Chile is technically free to enter into an alliance with other airlines because of the condition against enforcement of the American/Lan Chile exclusivity provision on marketing arrangements, the likelihood that Lan Chile would enter into a commercially-reasonable code-share agreement with another airline and reduce the market power of American/Lan Chile is exceedingly slim.

Antitrust immunity would increase the anticompetitive harm of the American/Lan Chile alliance, but it is only part of the problem, as American's alliances with TACA and other Latin American carriers demonstrate. The Department has recognized that American's overlapping alliances with Latin American partners raise "serious competitive questions" even when they do not involve antitrust immunity. (Order 97-1-15 at 6) Even without antitrust immunity, a code-share agreement between the dominant U.S. carrier (American) and the dominant Chilean carrier (Lan Chile) between the U.S. and Chile would create the same formidable barrier to competition that exists now under the highly restrictive U.S.-Chile bilateral aviation agreement. American and Lan Chile would exclude competitors by cooperating at American's Miami fortress hub and elsewhere without providing any truly new service options. This would allow American and its Latin American partners, including Lan Chile, to dominate other U.S.-South America markets as well. The tentative decision to approve and immunize the American/Lan Chile alliance is contrary to the public interest and should not be confirmed.

**III. THE CONDITIONS PROPOSED FOR THE AMERICAN/LAN CHILE ALLIANCE ARE INADEQUATE TO REMEDY THE ANTICOMPETITIVE IMPACT OF GRANTING ANTITRUST IMMUNITY AND SHOULD BE NO LESS RESTRICTIVE THAN CONDITIONS ON OTHER ALLIANCES**

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The Department's show-cause order places fewer restrictions and limitations on the American/Lan Chile alliance than have been imposed on other alliances. The Department should place greater restrictions on the American/Lan Chile alliance

since its anticompetitive impact, if approved, would be substantially greater than the anticompetitive impact of other alliances. At a minimum, the Department must ensure the American/Lan Chile conditions are no less restrictive than those placed on other alliances.

Unlike the restriction on the American/TACA alliance, the Department has not prohibited the American/Lan Chile alliance from having a joint alliance committee or sharing more information between carriers on current or prospective fares or seat availability than they make available to airlines and travel agents generally. (See Order 98-5-26 at 25-26)

The American/Lan Chile alliance is immunized for three years, which is one year more than the American/TACA alliance. (See Order 98-5-26 at 25) The Department has proposed no review of American/Lan Chile antitrust immunity after eighteen months, unlike conditions on the Delta/Swissair/Sabena/Austrian alliance. (See Order 96-6-33, Appendix A at 2) Moreover, the Department's exceptions to its U.S. point-of-sale passenger conditions are more liberal for the American/Lan Chile alliance than those allowed for other alliances since they include not only promotional fare products and corporate fare products but, in addition, consolidator/wholesaler fare products and group fare products. (See Order 96-6-33, Appendix A at 1)

While no conditions will remedy or ameliorate significantly the serious anticompetitive effects of the American/Lan Chile alliance, the Department should

at the very least tighten the conditions on the American/Lan Chile alliance by requiring American and Lan Chile to comply with the same level of restrictions it has previously placed on immunized alliances.

Specifically, if the Department approves or immunizes the American/Lan Chile alliance, the Department should add conditions prohibiting American and Lan Chile from having a joint alliance committee and engaging in any preferred information sharing activities on current or prospective fares or seat availability between the U.S. and South America. The Department's exceptions to its conditions on joint fare and capacity coordination involving U.S. point-of-sale passengers should be limited to the exceptions found in other alliance conditions. The American/Lan Chile agreement should be subject to renewal at two years, not three. In addition, the Department should require an eighteen-month review of the conditions on the American/Lan Chile alliance to ensure additional conditions are placed on the alliance if indicated by competitive conditions.

These additional conditions are essential as minimum measures since the American/Lan Chile alliance is highly anticompetitive and different from the Northwest/KLM and other European airline alliances. The eighteen-month review will ensure the Department will review the state of U.S.-Argentina opportunities and the competitive impact of the American/Lan Chile alliance on consumers and have an early opportunity to terminate antitrust immunity or add more effective conditions and restrictions on the American/Lan Chile alliance to increase

competition. A prohibition on preferred information sharing and joint alliance committee will also help to protect consumers since American and Lan Chile will not have those means of coordinating their anticompetitive activities.

#### IV. CONCLUSION

Confirming the tentative approval of the American/Lan Chile alliance would enable American and Lan Chile to block competition in the Southern Cone and throughout South America, resulting in serious harm to the public interest by achieving the core objective underlying American's agenda with Lan Chile, Aerolineas Argentinas and other Latin American carriers. The Department should deny or dismiss the American/Lan Chile request for approval of its alliance and for antitrust immunity. If the Department allows the American/Lan Chile alliance to proceed on any basis, it must impose the stronger restraints Continental has

proposed if competition in the Southern Cone region and throughout South America  
is to survive.

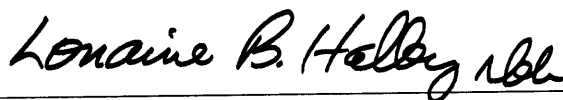
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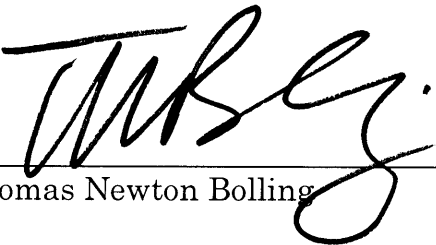
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May 20, 1999

CERTIFICATE OF SERVICE

I certify that I have this date served the foregoing document on American and Lan Chile and all parties to this proceeding in the manner specified in the Department's Rules of Practice.

  
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Thomas Newton Bolling

May 20, 1999

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