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Order 2000-11-23



UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION
OFFICE OF THE SECRETARY
WASHINGTON, D.C.

Issued by the Department of Transportation
on the 20th day of November, 2000

Served: November 21, 2000

*Los Angeles-San Jose del Cabo Exemption
Proceeding*

Docket OST-2000-8361 - 1

Application of

AMERICAN AIRLINES, INC.

for exemption pursuant to 49 U.S.C. Section
40109 (Los Angeles-San Jose del Cabo)

Docket OST-2000-7714 - 16

Application of

UNITED AIR LINES, INC.

for exemption pursuant to 49 U.S.C. Section
40109 and a statement of Authorization
pursuant to 14 C.F.R., Part 212 (Los Angeles-
San Jose del Cabo)

Docket OST-2000-7656¹ - 19

ORDER TO SHOW CAUSE

Summary

By this order we tentatively select American Airlines, Inc. (American), to provide foreign scheduled air transportation services between Los Angeles, California, and San Jose del Cabo, Mexico, pursuant to exemption authority.

¹ United's application in Docket OST-2000-7656 also sought exemption authority and a statement of authorization to provide seasonal services in the Los Angeles-Puerto Vallarta market, where it would place Mexicana's code on United's flights in the market. We granted that authority by Notices of Action Taken, dated August 4 and August 25 2000. This order deals only with United's Los Angeles-San Jose del Cabo request.

Background

Under the U.S.-Mexico aviation agreement, two U.S. carriers may be designated to serve a given city-pair route with their own aircraft (direct carrier services/operating authority). In addition, up to four U.S. carriers may hold authority to serve a given city-pair market pursuant to code-share arrangements (code-share only authority on flights operated by other carriers). Currently, Alaska Airlines, Inc. (Alaska), is the only U.S. carrier designated to provide direct services in the Los Angeles-San Jose del Cabo market, and Compania Mexicana de Aviacion, S.A. de C.V. (Mexicana) and Aero California S.A. de C.V. (Aero California) are the two Mexican carriers authorized to serve the market. Continental Airlines, Inc. (Continental), Northwest Airlines, Inc. (Northwest), and United each holds code-share only authority to serve the route.² Thus, one operating designation remains available, and one code-share only authorization remains available for Los Angeles-San Jose del Cabo services.

Applications

On July 14, 2000, United filed an application, in Docket OST-2000-7656, for, among other things, exemption authority to provide direct carrier services in the Los Angeles-San Jose del Cabo market. On July 31, 2000, American filed a competing application, in Docket OST-2000-7714, for exemption authority to provide direct carrier services in the market. In response to the competing application filed by American, United filed a motion to consolidate the applications of United and American for Los Angeles-San Jose del Cabo authority, and to set down an expedited carrier selection case in this matter. We received no other competing applications or any opposition to United's motion.³

Both United and American propose to offer daily service in the Los Angeles-San Jose del Cabo market.⁴ United proposes to commence service on December 16, 2000, using 138-seat Airbus 320 aircraft. In addition to the necessary exemption authority for this service,⁵ United also seeks route integration authority to combine the San Jose del Cabo service with its other certificate and exemption authority, and seeks a statement of authorization to display Mexicana's airline code on United's flights to provide reciprocal code-share services.

American proposes to begin service on November 1, 2000, using 129-seat MD-82 aircraft. In addition to the proposed daily service, American also proposes to operate an additional once-

² Northwest and Continental code share on flights operated by Alaska in the Los Angeles-San Jose del Cabo market, and United code shares on flights operated by its partner, Mexicana.

³ In response to United's motion, Delta Air Lines, Inc., stated that it was also interested in providing direct carrier services in the Los Angeles-San Jose del Cabo market. (Answer of Delta to Motion of United for Consolidation and Request for Immediate Action dated August 4, 2000). However, on August 11, 2000, Delta filed a pleading stating that it had determined not to pursue the authority at this time. By notice dated August 11, 2000, the Department requested that new applications or amendments to existing applications be filed no later than August 14, 2000, with answers due no later than August 23, 2000, and replies due no later than September 1, 2000. No additional applications were filed.

⁴ Both applicants revised their service proposals following submission of their original applications. The information given here reflects their revised proposals.

⁵ United currently holds code-share only authority in the Los Angeles-San Jose del Cabo market, where it places its code on the flights of Mexicana. In its application, United seeks, among other things, to convert the code-share only authority into operating exemption authority to provide services with its own aircraft.

weekly flight on Saturdays on a seasonal basis during the period December 15, 2000, through April 30, 2001.

Responsive Pleadings

Each of the applicants submitted an answer to the other's application and each filed a reply.

American maintains that it will provide a superior service pattern in this case, stating that it will start service in the market first (November 1, 2000, vs. December 16, 2000), and that it will provide additional service during the seasonal period. American argues that United already has on-line access to the Los Angeles-San Jose del Cabo market through its alliance partner Mexicana, and that, in the interest of maximizing competition, the Department should award to American its first opportunity for on-line service in the market. American argues that passengers to San Jose del Cabo from points outside of Los Angeles already have many connection opportunities through other gateways (Chicago, Dallas/Ft. Worth, Denver, Houston, Minneapolis/St. Paul, Phoenix, San Francisco, San Diego, San Jose, and Seattle) and, thus, the Department should weigh more heavily the merits of each applicant's proposal in the large local market in this case, rather than relying on connecting service which is already available. American argues that only American is in a position to compete with both United/Mexicana and Alaska (the largest Los Angeles-San Jose del Cabo carrier),⁶ and that United's selection here would bring no new competitive brand to the market.⁷ American argues further that it is the only carrier attempting a significant challenge to United's dominance at Los Angeles, and that the Department should not grant limited-entry authority to United that would serve only to enhance its dominant position at Los Angeles, contrary to the public interest in having multiple strong competitors at major U.S. airports.

American also argues that United has greatly exaggerated the benefits of United's proposal in this case by overstating its southbound and northbound connecting claims. In this regard, American notes that United has listed a number of connecting cities that have connecting times in excess of four hours (some more than 15 hours). American argues further that, while United claims that only United's proposal will serve 13 additional western communities (not served by American), the 13 subject communities account for just 525 annual San Jose del Cabo bookings, or only 1.4 passengers per day each way.⁸ American maintains that both American and United would offer nonstop or single-connecting service to San Jose del Cabo from the 10 largest markets for such service, and that United's claim of on-line connecting service to 63 cities versus American's on-line connecting service to 47 cities is "hardly a decisive selection factor in a market" where local passengers predominate. American maintains that, under these circumstances, the Department's goal here should be to ensure that the public has multiple on-line options for travel between Los Angeles and San Jose del Cabo.

⁶ Currently, Alaska operates three daily flights in the market. It also supplements this service with three additional weekly flights that are not operated on a daily basis.

⁷ American maintains, however, that, to the extent that flow traffic is important, American also provides nonstop service to Los Angeles from a number of major cities in the western United States with significant traffic to San Jose del Cabo, including San Diego, San Francisco, San Jose, Oakland, Phoenix, Las Vegas, and Denver. American states that it will also offer on-line service to smaller cities in California, including Bakersfield, Fresno, Monterey, Palm Springs, San Luis Obispo, and Santa Barbara.

⁸ American reply at 6.

United states that its proposal offers a considerably broader and more inclusive view of how new hub online nonstop Los Angeles-San Jose del Cabo service can benefit the most U.S. passengers in cities and communities both within and beyond the Los Angeles metropolitan area, making United's proposal superior in terms of benefits to both the local city-pair market and connecting markets. United argues that as Los Angeles' only hub carrier, United is much better positioned than American to offer superior service to local Los Angeles passengers, and that United's hub will enable United to deliver new on-line one-stop connecting service to San Jose del Cabo from more cities and communities, including many in the western states that are poorly served.⁹ United argues further that, because the Los Angeles-San Jose del Cabo market already enjoys competitive nonstop service offered on a daily basis by three carriers (Alaska Airlines, AeroCalifornia, and Mexicana), it is more important that the fourth competitor have the staying power to compete with the incumbents. United maintains that it will provide more seats annually in the large local Los Angeles-San Jose del Cabo market,¹⁰ and that it is better placed than American to capture a substantial share of, and to further develop, that market. United maintains that its hub traffic feed will enhance its ability to grow the market and add more daily capacity over time, further improving United's ability to compete with Alaska and expand consumer choices. United also states that its hub-and-spoke network in the western states provides both a strong foundation for service in cities not now well served to San Jose del Cabo, and a springboard for further development of the market. United argues that many of American's more limited connections would involve self-diversion of traffic currently connecting to San Jose del Cabo via American's hubs at Chicago and Dallas/Ft. Worth.

United further states that selection of United in this case will increase competition in the U.S.-Mexico market generally.¹¹ In this regard, United states that American already has ample access to the Mexico market through its hubs at Dallas/Ft. Worth, Chicago, and Miami, and does not need additional service from Los Angeles, where it does not operate a hub. United argues that American has failed to mention that it has a code-share relationship with Alaska Airlines. United states that, while to date, American and Alaska have not implemented any code-sharing services on each other's Mexico services, there is nothing in the U.S.-Mexico aviation agreement restricting their ability to do so. United argues that it would be unfair and inimical to competition to disqualify United from adding an important new service to Mexico using its own equipment in order to accommodate American, which is the largest U.S. carrier to Mexico, and Alaska's code-share partner.

Tentative Decision

We have tentatively decided to select American to provide foreign scheduled air transportation services in the Los Angeles-San Jose del Cabo market.

⁹ United also states that its proposal is enhanced by United's ability to offer the flexibility of a second daily flight in conjunction with Mexicana, providing for stronger competition against Alaska.

¹⁰ American proposes 385 flights annually, with a total of 49,665 seats; United proposes 365 flights annually, with a total of 50,370 seats (Exhibit UA-Ans.-6).

¹¹ United argues that American is the largest U.S. carrier in terms of U.S.-Mexico Computer Reservation Service (CRS) bookings and U.S.-Latin American departures and enplanements; and that United ranks just 5th, 4th, and 4th among U.S. carriers in these respective categories (United answer at 9, and Exhibits UA-Ans.-17, 18, and 19).

In reaching a tentative decision here, our principal objective is to maximize the public benefits that will result from award of the authority at issue. In this regard, we have considered which applicant will most likely offer and maintain the best service for the traveling and shipping public and would best promote competition in the Los Angeles-San Jose del Cabo market.

Given these objectives, we have carefully examined the proposals of both United and American, and tentatively conclude that American's proposal would provide the greater combination of service and competitive benefits in this case. American would provide daily service in the Los Angeles-San Jose del Cabo market, serving both the large local market and connecting traffic that may use Los Angeles as a gateway to San Jose del Cabo. Significantly, American would be a new entrant to the Los Angeles-San Jose del Cabo market and, thus, would better enhance intragateway competition as well as the U.S. carrier position in this market.

In terms of service benefits, the proposals of American and United are comparable with respect to service, capacity, and frequency and, thus, we do not find that either carrier has a decisive advantage over the other in this regard. Both American and United propose well-timed flights to compete with services already offered in the market by the incumbent carriers, Alaska, Mexicana, and Aero California. Both carriers propose to use similarly sized aircraft, with United using 138-seat Airbus A320 aircraft, and American using 129-seat MD82 aircraft. Both are prepared to commence service for the coming winter season. In addition, both American and United would offer regular once-daily nonstop year-round service in the market. While United's proposal offers slightly more capacity on an annual basis as a result of its larger aircraft, American would provide an additional frequency and capacity during the winter season. In these circumstances, we tentatively find that neither carrier proposal for serving the local market either provides it with significant advantages or outweighs other important carrier selection factors in this case.

Furthermore, we also tentatively find that both of the applicants are in a position to serve the local market as well as connecting passengers that would use Los Angeles as a gateway to San Jose del Cabo. To the extent that connecting passengers would use Los Angeles as a gateway, both applicants offer well-timed flights to provide on-line connections to San Jose del Cabo via Los Angeles to and from a number of cities in California, as well as the western U.S. While United has argued that its proposal is superior because it would offer more on-line connections overall than American, we do not find this argument persuasive in this case.¹² Thirteen cities throughout the United States currently receive nonstop service to San Jose del Cabo, including several in the western United States, offering numerous connecting gateways for San Jose del Cabo passengers.¹³ Moreover, of the 10 largest U.S.-San Jose del Cabo markets cited by United, both carriers provide online services to the majority of the cities, offering reasonable connections to their proposed Los Angeles-San Jose del Cabo services.¹⁴ Further, as American notes, and not

¹² United has stated that its proposal will offer online single connecting San Jose del Cabo service to as many as 63 cities behind its Los Angeles hub (Exhibit UA-Ans-2). American has stated that its proposal will offer online single connecting service to as many as 47 cities (see American answer at 6).

¹³ The current U.S.-San Jose del Cabo direct nonstop services are as follows: Chicago, Dallas/Ft. Worth, Denver, Los Angeles, San Diego, San Francisco, San Jose, Seattle, Phoenix, Houston, Minneapolis/St. Paul, New York, and Atlanta.

¹⁴ Top 10 markets as reflected by United Exhibit UA-12, page 1 of 1 (Los Angeles, San Francisco, Seattle, Phoenix, San Diego, Portland, Chicago, Dallas/Ft. Worth, Denver, and Houston). Source: Daily CRS Bookings, U.S./Canada-SJD, 12 months ended July 2000.

refuted by United, the 13 western cities to which United would offer online service, and American would not, account collectively for fewer than two daily bookings in each direction.¹⁵ Thus, while United would offer on-line connecting service to more cities overall, we are unpersuaded that the difference is decisive.

However, when we turn to an analysis of the applicants' respective competitive benefits, we tentatively find that American has a clear advantage. United now serves the Los Angeles-San Jose del Cabo market under its code-share arrangement with Mexicana, and since there are no frequency limitations on services provided under the U.S.-Mexico aviation agreement, United is free to increase this service in conjunction with its partner in response to market demand. On the other hand, American does not now serve Los Angeles-San Jose del Cabo and would be a new entrant to the market. The Department has consistently found that new entry is a significant carrier selection factor because it provides consumers with new service options and incumbents with new incentives to provide consumers with service that meets their needs. The record in this case shows that the selection of American would provide these important public benefits. American's selection here would enable five U.S. carriers to serve the market, enhancing competition among the U.S. carriers serving the gateway either with direct service or under code-share arrangements with other carriers. Thus, selection of American would help ensure that the limited competitive opportunities under the U.S.-Mexico aviation agreement are fully used, providing the broadest range of carrier services and choice in the Los Angeles-San Jose del Cabo market, benefits not available under United's proposal. In these circumstances, we tentatively find that, on balance, the considerations favoring the selection of American outweigh those favoring United.

In reaching this tentative conclusion, we have carefully considered United's argument that authorizing United to provide direct carrier services in the market offers greater competitive benefits than authorizing American because United would be a stronger competitor to Alaska, the dominant carrier in the market. United asserts that were it able to operate direct service, it would be able to offer a greater frequency of service in competition with Alaska. However, as noted above, United already has the ability to offer greater frequency of service under its code-share arrangement with Mexicana. The selection of American in this case would provide new effective competition for Alaska and all airlines serving the market, including United.¹⁶

That said, it would be our preference to authorize the services of both American and United here. We will continue our diplomatic efforts toward broader liberalization of the U.S.-Mexico aviation agreement so that all U.S. carriers that are interested in serving the U.S.-Mexico market can do so without limitation. In the meantime, should we obtain approval from the Mexican Government for additional operating designations in the subject market, we would act immediately to authorize the services of interested carriers. Indeed, we have provided streamlined procedures for U.S. carriers to convert their code-share only authorizations to direct carrier authorizations, such as United seeks here, and United has recently converted some of its other U.S.-Mexico services.¹⁷

¹⁵ American Exhibit, AA-R-4.

¹⁶ With respect to United's arguments that American and Alaska have a code-share relationship, we note that American and Alaska do not now provide any code-share services in the U.S.-Mexico market, nor have the carriers indicated any future plans to do so.

¹⁷ See Notices of Action Taken dated August 4, and August 25, 2000.

We intend to complete this case quickly to accommodate the carriers' future plans to the extent possible. Therefore, we will require that objections to our tentative decision here be filed no later than 10 days from the date of service of this order, and that answers to such objections be filed no more than seven calendar days thereafter. Given our desire to expedite this case, we will authorize service of documents by facsimile and by electronic mail.¹⁸ Parties that are interested in such service, however, should state if they want service by email or fax and should provide interested parties with their FAX numbers and/or email addresses.

ACCORDINGLY,

1. We institute the *Los Angeles-San Jose del Cabo Exemption Proceeding*, Docket OST-2000-8361, to select a U.S. carrier to provide foreign scheduled air transportation services of persons, property, and mail between Los Angeles, California, and San Jose del Cabo, Mexico;
2. We consolidate the applications of American Airlines, Inc., in Docket OST-2000-7714; and United Air Lines, Inc., in Docket OST-2000-7656 (to the extent United seeks Los Angeles-San Jose del Cabo authority), into the *Los Angeles-San Jose del Cabo Exemption Proceeding*, in Docket OST-2000-8361, for contemporaneous consideration;
3. We tentatively select American Airlines, Inc., for exemption authority to provide foreign scheduled air transportation services of persons, property, and mail between Los Angeles, California, and San Jose del Cabo, Mexico;
4. We direct any interested parties objecting to our tentative decision in this order to file such objections with the Department, Dockets, Docket OST-2000-8361, U.S. Department of Transportation, 400 Seventh Street, S.W., Washington, D.C. 20590, and serve on all parties to this proceeding within 10 days of the service date of this order, and that any replies to such objections be filed no later than seven calendar days thereafter;
4. If timely and properly filed objections are filed, we will give full consideration to such pleadings before making a final decision; if no objections are filed, we will deem all further procedural steps waived and will proceed immediately to a final decision making final the tentative decision set forth in this order;¹⁹
5. We grant the motion of United Air Lines, Inc., requesting consolidation of the applications filed by American in Docket OST-2000-7714, and United in Docket OST-2000-7656, into the *Los Angeles-San Jose del Cabo Exemption Proceeding*;
6. To the extent not granted or tentatively granted, we tentatively deny all requests in the newly established docket; and

¹⁸ The original filing of any comment, objection, or answer should be on 8½" x 11" white paper using dark ink and be unbound, without tabs, which will expedite use of our docket imaging system. In the alternative, filers may use the electronic submission capability available through the Dockets DMS Internet site (<http://dms.dot.gov>) by following the instructions on the web site.

¹⁹ Since we have provided for objections to our tentative decision, we will not entertain petitions for reconsideration of this order.

7. We will serve a copy of this order on American Airlines, Inc.; Delta Air Lines, Inc.; United Air Lines, Inc.; the U.S. Department of State (Office of Aviation Negotiations); and the Ambassador of Mexico in Washington, D.C.

By:

SUSAN MCDERMOTT
Deputy Assistant Secretary for Aviation
and International Affairs

(SEAL)

An electronic version of this order is available on the World Wide Web at:
http://dms.dot.gov/reports/reports_aviation.asp