The American Antitrust Institute

September 22, 2015

William J. Baer
Assistant Attorney General
U.S. Department of Justice Antitrust Division
950 Pennsylvania Avenue NW
Washington, D.C. 20530

Re: Broadening the Lens on Investigating Potential Collusion in the U.S. Airline Industry

Dear Assistant Attorney General Baer:

The American Antitrust Institute (AAI) has been active in supporting a strong antitrust enforcement response to impediments to competition in the U.S. airline industry.[1] This includes mergers, potentially exclusionary behavior, and coordinated conduct that could harm competition and consumers. AAI's advocacy has spanned all aspects of the airline industry, including the distribution of airfares and services to consumers. Competition in the domestic airline industry has taken a beating in the last decade. Extensive consolidation, a relatively closed domestic travel market, and the airlines' strategic integration into their own dedicated distribution channels are among the contributing factors.

The foregoing changes raise numerous questions that bear materially on the U.S. Department of Justice (DOJ) probe into potential collusion by the airlines. The AAI commends the DOJ for initiating this inquiry and encourages the Antitrust Division to take a broad "lens," namely by scrutinizing both price *and* non-price dimensions of competition involving the "Big 4" carriers—United, Delta, American, and Southwest.

Potential anticompetitive coordination is not limited to capacity "discipline" to maintain supracompetitive fares. It is also important to consider parallel conduct involving fees for ancillary services and on certain "rules" of commerce. The latter include policies and strategies that could impair competition from the rival distribution channels that are critical for promoting transparency and comparison-shopping. These strategies could include "standardized" distribution models, surcharges on itineraries not purchased through the airlines' own websites, and prohibitions on third-party intermediary access to airline data.

The first part of this letter briefly summarizes the fundamental changes in the domestic airline industry over the last decade that give rise to concerns over potential collusion among the Big 4

[1] The AAI is an independent non-profit education, research, and advocacy organization. Its mission is to advance the role of competition in the economy, protect consumers, and sustain the vitality of the antitrust laws. For more information, see www.antitrustinstitute.org. Many thanks to AAI Research Fellow, Kyle Virtue, and former AAI Research Fellow, Birzhan Batkeyev, for research assistance.

carriers. The latter part examines opportunities for potential coordinated conduct that the AAI believes should also be scrutinized.

I. From Ten to Four in a Decade: Consolidation in U.S. Airlines

In the last decade, the U.S. airline industry has experienced a host of challenges: limits to organic growth, fuel price volatility, and slowing demand for air travel.[2] Legacy carriers have responded to these developments with bankruptcies, new pricing and ancillary fee strategies, and changes in distribution policies. Consolidation among airlines, however, has been the most sought after tonic for the rough life of a competitor. There have been five major mergers in the last decade: US Airways-America West Airlines (2005); Delta Air Lines-Northwest Airlines (2008); United Airlines-Continental Airlines (2010); Southwest Airlines-AirTran Airways (2011); and US Airways-American Airlines (2013).[3] Today, American is the largest U.S. carrier with a market share of 20%. It is followed by Southwest with 18%, Delta with 17%, and United with 15%.[4] The Big 4 control about 70% of the national market.

A. Direct Evidence of Competitive and Consumer Harm

At the time of the major mergers, direct evidence was available to show that further consolidation would likely harm competition and consumers. One of the least-recognized examples is Southwest's acquisition of low cost carrier (LCC) AirTran. A 2010 AAI white paper explained that AirTran had a history of strategically entering and exiting Southwest's markets in the quest for market share.[5] The merger thus eliminated AirTran as a head-to-head competitor to Southwest. AirTran's disruptive behavior also likely had a disciplining effect on the market and the loss of this LCC "maverick" eliminated competition that could have disrupted any anticompetitive coordination among carriers.

Fare increases and capacity cutbacks in the wake of the Delta-Northwest and United-Continental mergers are well documented.[6] The "Southwest effect" is long gone, as the airline has grown, become dominant at numerous secondary airports, and prices largely under the umbrella of the legacy carriers.[7] The government's complaint in US Airways-American revealed evidence of competitive and consumer harm from previous airline mergers, particularly from potential coordination. It explained, for example, that in recent years "the major airlines have, in tandem,

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[2] *See, e.g.*, Severin Borenstein, *Why U.S. Airlines Need to Adapt to a Slow-Growth Future*, Bloomberg, June 3, 2012, http://www.bloomberg.com/news/2012-06-03/why-u-s-airlines-need-to-adapt-to-a-slow-growth-future.html.

[3] No remedies were required in the first four mergers. In US Airways-American, the DOJ recognized the systemic problems caused by prior consolidation and brought a robust complaint to block the merger, but it ultimately settled for remedies limited to targeted slot and gate divestitures that have not proven to have fully restored the competition lost by the merger.

[4] Shares are measured by revenue passenger-miles. U.S. Dep't of Transp., Bureau of Transp. Statistics, *Airline Domestic Market Share: July 2014–June 2015* (2015), http://www.transtats.bts.gov.

[5] Diana L. Moss, Am. Antitrust Inst., *Competition at a Crossroads: Southwest Airlines and AirTran Airways* 18 (2010), *available at* http://www.antitrustinstitute.org/sites/default/files/SouthwestAirTran%20White%20Paper.pdf.

[6] *See, e.g.*, Volodymyr Bilotkach & Paulos Ashebir Lakew, *On Sources of Market Power in the Airline Industry: Panel Data Evidence from the US Airports*, 59 Transp. Pol'y Part A: Pol'y & Prac. 288 (2014), *available at* http://www.sciencedirect.com/science/article/pii/S0965856413002371. The authors show welfare losses in over 30 small airports resulting from the Delta-Northwest merger. *See also* Diana L. Moss & Kevin Mitchell, Am. Antitrust Inst. & Bus. Travel Coal., *The Proposed Merger of US Airways and American Airlines* 11 (2012), *available at* http://www.antitrustinstitute.org/sites/default/files/AAI_BTC_USAir-AA_White%20Paper_8-7.pdf.

[7] S*ee, e.g.*, John Kwoka, Kevin Hearle & Phillippe Alepin, *Segmented Competition in Airlines: The Changing Roles of Low-Cost and Legacy Carriers in Fare Determination* (2013) (publication forthcoming), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2212860.

raised fares, imposed new and higher fees, and reduced service. Competition has diminished and consumers have paid a heavy price."[8]

B. The Myth of Merger-Related Efficiencies

Had claimed efficiencies in previous mergers materialized as promised, lowering costs and increasing consumer benefits, the competitive concerns that now pervade the industry would likely not be the subject of federal antitrust scrutiny. In 2013, the AAI conducted a retrospective analysis of claimed efficiencies in airline mergers.[9] The analysis found that system integration (e.g., combining reservation and IT systems and workforces) in some past mergers has been difficult, protracted, and more costly than what was predicted by the airlines when they made their case to antitrust enforcers.[10] These problems in some cases continue long after mergers are consummated, particularly for United-Continental.[11]

The AAI study also noted that over the last decade, airlines shifted efficiencies claims from easier to verify cost-savings to much harder-to-verify, elusive network benefits such as increased "connectivity."[12] The AAI study found, for example, that pre- to post-merger, Delta-Northwest cut 11% of airport pairs from its network, United-Continental cut 9%, and Southwest-AirTran cut 22%.[13] Many of these cuts affected smaller and medium size communities that lie behind major hubs.[14]

The Big 4 carriers' limited ability to realize claimed efficiencies in past mergers has imposed additional costs on consumers in the form of loss of service, inconvenience, and a generally more difficult traveling experience. Part of the degradation in U.S. air travel may also be due to the fact that LCCs are less able to provide competitive discipline in a market dominated by the Big 4 carriers. LCC delays, for example, have increased substantially over the last decade, with spikes in 2008 and 2012.[15] This trend may be explained by congestion externalities associated with the dominance of the Big 4 at their hubs, heightened incentives to create delays for smaller LCC rivals, or pressures for LCCs to bracket flights around those of the network carriers (as opposed to scheduling in off-peak times) in order to compete more effectively.[16] These effects also shrink consumer benefits and welfare.[17]

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[8] Amended Complaint at 3, *United States v. US Airways Grp., Inc.*, 979 F. Supp. 2d 33 (D.D.C. 2013), *available at* http://www.justice.gov/file/514521/download [hereinafter US Airways DOJ Complaint].

[9] Diana L. Moss, Am. Antitrust Inst., *Delivering The Benefits? Efficiencies And Airline Mergers* (2013), *available at* http://www.antitrustinstitute.org/content/aai-issues-white-paper-delivering-benefits-efficiencies-and-airline-mergers.

[10] *Id.* at 2.

[11] Christopher Drew, *United Airlines Grounds Flights: Citing Computer Problems*, N.Y. Times, July 8, 2015, http://www.nytimes.com/2015/07/09/business/united-airlines-grounds-flights-citing-computer-glitch.html?_r=0.

[12] *See Delivering the Benefits?*, *supra* note 9, at 4. *See also* John Kwoka, *The Changing Nature of Efficiencies in Mergers and in Merger Analysis,* 60 Antitrust Bull. 231 (2015).

[13] *Delivering the Benefits?*, *supra* note 9, at 13.

[14] *See also* Jack Nicas, *Airline Consolidation Hits Smaller Cities Hardest*, Wall St. J., September 10, 2015, http://www.wsj.com/articles/airline-consolidation-hits-smaller-cities-hardest-1441912457.

[15] *Delivering the Benefits?*, *supra* note 9, at 15.

[16] *Id.* at 16.

[17] Cost savings from merger-related efficiencies are not, of course, the same as those generated from capacity and service cutbacks which are related to the exercise of market power post-merger.

II. Reshaped Competition in U.S. Airlines: Capacity Tightening and a Return to Profitability

A. Fares, Fuel, and Margins

Statistics for the carriers that now make up the Big 4, across the hubs they have operated over the last decade, reveal the fundamental reshaping of the U.S. industry that has likely given rise to the DOJ's concerns over potential coordination. We looked at three years—2004, 2009, and 2014—to bracket the period of the time between the first merger of U.S. Airways-America West in 2005, the last merger of US Airways-American in 2013, and one year in the middle. Without attempting more complex economic analysis to determine if and when there were structural changes over the decade, we look simply at two five-year periods.

Average real fares across hubs declined almost 12% from 2004–2009. The 2008 recession, softening demand for air travel, and excess capacity were probably the drivers for this trend. Notably, however, fares fell over this period even as real fuel costs *increased* by 33%.[18] Given that fuel costs are a significant portion of total operating costs, this inverse relationship emphasizes the exposure that fares have to broader economic forces, as well as competition in the industry. Operating margins were -1.1% in 2004, increasing to only 1.6% by 2009.[19] The first five years of the decade of consolidation thus reveal a state of disarray in the domestic industry, with falling fares, increasing fuel costs, and negative operating margins.

The airlines' misery between 2004–2009 disappeared in the second half of the consolidation period. From 2009–2014, for example, the increase in average fares across hubs was 15%. This rate of growth far outstripped that of fuel costs, which slowed to less than 5% over the second period. Indeed, four of the five years from 2009–2014 were marked by *flat or declining* fuel costs for the Big 4. By 2014, operating margins had increased to 8.6% and the airlines were strongly profitable.[20] This second period includes the three mergers of United-Continental, Southwest-AirTran, and US Airways-American. Significantly higher fares and slower rates of increase in fuel costs, and strong return to profitability marked this phase.

The foregoing adjustments all occurred against the backdrop of highly concentrated markets. Average market concentration across hubs from 2004-2014 was between about 3,400 to 3,750 HHI.[21] While we do not see substantial increases in average market concentration across hubs, we

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[18] Fares obtained from U.S. Dep't of Transp., Bureau of Transp. Statistics, *Average Domestic Airline Itinerary Fares By Origin City, Ranked by Total Number of Domestic Passengers in 2014* (2015), *available at* http://www.transtats.bts.gov/AverageFare/. Fares are ticket prices at the time of purchase and have been deflated by the Consumer Price Index (CPI) (2014=100). Market concentration derived from U.S. Dep't of Transp., Bureau of Transp. Statistics, *Air Carriers: T-100 Domestic Market (U.S. Carriers)* (2015), *available at* http://www.transtats.bts.gov/DL_SelectFields.asp?Table_ID=258&DB_Short_Name=Air%20Carriers.

[19] U.S. Dep't of Transp., Bureau of Transp. Statistics, *U.S. Airline Industry Operating Margins: 2004-2010* tbl.3-9 (2010), *available at* http://www.rita.dot.gov/bts/sites/rita.dot.gov.bts/files/publications/transportation_statistics_annual_report/2010/html/chapter_02/table_03_09.html. Fuel costs derived from U.S. Department of Transportation, Bureau of Transportation Statistics, *Air Carrier Financial: Schedule P-12(a)*, *available at* http://www.transtats.bts.gov/DL_SelectFields.asp?Table_ID=294&DB_Short_Name=Air%20Carrier%20Financial. Fuel costs are calculated from fuel consumption and fuel cost for total scheduled domestic service, and have been deflated by the CPI (2014=100).

[20] Press Release, U.S. Dep't of Transp., Bureau of Transp. Statistics, 2014 Airline Financial Data (May 5, 2015), *available at* http://www.rita.dot.gov/bts/press_releases/bts022_15.

[21] U.S. Dep't of Justice & Fed. Trade Comm'n, *Horizontal Merger Guidelines* §11 (August 2010), *available at*

know that at the route level, significant increases in concentration (including some 3-2 and 2-1 mergers) were observed in the wake of the airline mergers that created the Big 4.[22]

B. Capacity Tightening

Even at an aggregate level, the foregoing results clearly depict the transformation of the domestic industry from a gaggle of "undisciplined" and unprofitable carriers, into a tight oligopoly of powerful airlines with significantly more control over fares and capacity. The fact that the Big 4 were raising fares in light of absolute decreases in fuel costs over much of 2009–2014 is inconsistent with normal business behavior. Delta CEO Richard Andersons' comment is revealing:

> It's wonderful that fuel has run down–we love it. There's a $2 billion opportunity out there if we hold fare levels constant. But over the very long-term horizon, it's just more conservative and prudent to use a high fuel assumption when you're buying airplanes or making other investments, and then when it comes in lower, hang on to all of it.[23]

Needless to say, a CEO facing vigorous competition would not have the luxury of holding fare levels constant in the face of falling input prices. Other forces were at work, notably a gradual but substantial tightening of capacity by the Big 4; by 10 percentage points over a 10-year period. Domestic load factor for the airlines that now comprise the Big 4 was 76% in 2004, increased to 82% in 2009, and to 86% in 2014.[24] This capacity discipline includes both higher aircraft load factors and cutbacks in service to smaller, behind-the-hub communities.

In recent years, airline CEOs have allegedly signaled each other about the benefits of capacity discipline to support fares. Whether these public exchanges on investor calls and through the press, or other nonpublic evidence, support a case for unlawful collusion has yet to be determined. A CEO that says that he or she will raise capacity by, say 2% percent next year is likely on solid legal ground. But a CEO that says that he or she will hold capacity increases to 2%, *so long as others do*, has potentially solicited collusive behavior. The conditionality of such a capacity strategy also exceeds the bounds of normal business behavior.

Other theories behind the potentially anticompetitive nature and causes of capacity discipline focus on asset management firms' ownership stakes in multiple airlines. For example, an institutional shareholder that holds shares in both United and Delta could have incentives to discourage carriers from competing hard because such competition would reduce their profits across the board.[25] One analyst highlighted just this undercurrent in the industry:

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http://www.justice.gov/atr/public/guidelines/hmg-2010.Pdf.

[22] Moss & Mitchell, *supra* note 6, at 15–16.

[23] Zainab Mulldalal, *The airline executives standing between you and cheap plane tickets*, Quartz, Jan. 13, 2015, http://qz.com/324981/the-airline-executives-standing-between-you-and-cheap-plane-tickets/. We note that there is an economic literature on the relative speeds of adjustment in crude oil versus refined petroleum products.

[24] Global Airline Indus. Program, *Traffic and Capacity by Operating Region, Domestic Load Factor*, MIT, *available at* http://web.mit.edu/airlinedata/www/2014%2012%20Month%20Documents/Traffic%20and%20Capacity/Domestic/Domestic%20Load%20Factor%20.htm. 6% of the total increase in domestic system load factor was achieved from 2004–2009. Incremental capacity discipline from 2009–2014 advanced at a slower rate (4%), likely because tightening capacity at higher load factors is more costly than at lower load factors.

[25] *See* Einer Elhauge, *Horizontal Shareholding As An Antitrust Violation* (Harvard John M. Olin Discussion Paper Series Paper No. 834, July 2015).

> …Delta skirmished with Wall Street in October 2014 during the carrier's third-quarter earnings call, when CEO Richard Anderson snapped at analysts questioning capacity growth, declaring, "It is not appropriate for the analyst community to be engaging in what forward capacity and pricing decisions are at Delta." It seemed as if Delta was telling the analysts: "Don't tell us how to run our airline."[26]

III. Potential Coordination: Ancillary Fees and Distribution Policies

A. Ancillary Fees

Rapidly growing airline ancillary fee revenues boosted profitability during the period from 2009–2014. Between 2009 and 2014, real ancillary fees reported by airlines worldwide grew on average at about 22% per year.[27] In its complaint in US Airways-American, the DOJ noted that concentration in the airline industry facilitates coordination in ancillary fees:

> Increased consolidation has likely aided the implementation of these fees. Indeed, the levels of the ancillary fees charged by the legacy carriers have been largely set in lockstep. One airline acts as the "price leader," with others following soon after. Using this process, as a US Airways strategic plan observed, the airlines can raise their fees without suffering "market share impacts."[28]

Moreover, the complaint explained that coordination on ancillary fees was a likely outcome of the US Airways-American merger. "If not stopped, the merger would likely substantially enhance the ability of the industry to coordinate on fares, ancillary fees, and service reductions by creating, in the words of US Airways executives, a 'Level Big 3' of network carriers, each with similar sizes, costs, and structures."[29]

The AAI encourages the DOJ to consider the effect of potential coordination among the Big 4 carriers on ancillary fees. For example, baggage fees are the second largest category of ancillary fee revenue—about 25% of the total—and have already been the subject of concerns over potential parallel behavior.[30] For example, when American began charging for the first checked bag in May 2008, both United and US Airways followed within about three weeks.[31] According to press reports, Delta Air Lines announced higher baggage fees on January 11, 2010. Within days, Continental, United, US Airways, and American matched the higher fees.[32]

We collected data on baggage fee revenues charged by the Big 4 to highlight similarities in carrier movements over the latter half of the consolidation decade, as shown in Figure 1. Southwest is not

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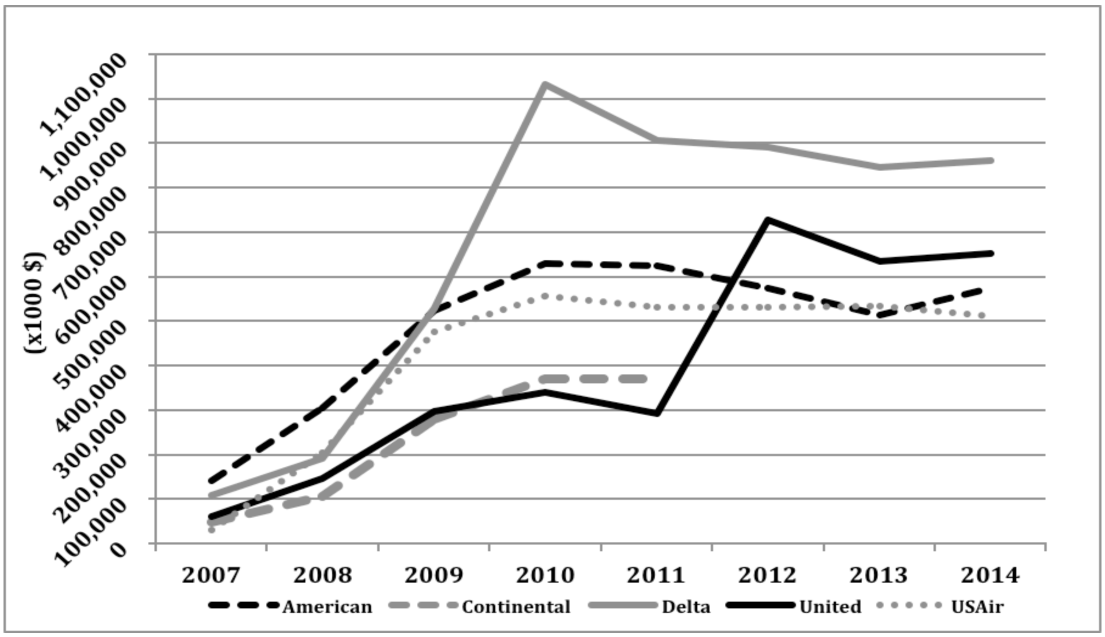
[26] Ted Reed, *American CEO's Pay Gesture Shows Wall Street Runs the Airline Industry*, AFACWA, April 27, 2015, http://www.afacwa.org/american_ceo_s_pay_gesture_shows_wall_street_runs_the_airline_industry.
[27] Jay Sorensen, IdeaWorks Co., *Ancillary Revenue Report for 2015: The CarTrawler Yearbook of Ancillary Revenue* 5 (2015), *available at* http://www.ideaworkscompany.com/wp-content/uploads/2015/09/2015-Ancillary-Revenue-Yearbook.pdf.
[28] US Airways DOJ Complaint, *supra* note 8, at 27.
[29] *Id.* at 4. *See also id.* at 17, 14.
[30] Press Release, IdeaWorks Co., Airline Ancillary Revenue Projected to be $49.9 Billion Worldwide in 2014 (2013), *available at* http://www.ideaworkscompany.com/wp-content/uploads/2014/11/Press-Release-92-Global-Estimate.pdf.
[31] US Airways DOJ Complaint, *supra* note 8, at 27. The government's complaint also noted that over a period of two weeks in Spring 2013, United, Delta, US Airways, and American all increased their ticket change fee for domestic travel from $150 to $200.
[32] Jay Sorenson, IdeaWorks Co., *U.S. Airlines Will Generate Millions from Higher Baggage Fees* 1 (2010), *available at* http://www.ideaworkscompany.com/wp-content/uploads/2012/05/2010-Baggage-Fee-Millions.pdf.

shown since the airline has pursued a different bag policy fee than the other large carriers. We note that bag fee revenues are not bag fees themselves and that our analysis also does not attempt to examine any sequential behavior surrounding bag fee hikes. The data nonetheless flag what appear to be common movements across carriers that could warrant additional scrutiny. Periods of similar directional movement in baggage fee revenues are not difficult to identify.[33] All airlines saw positive rates of growth in baggage fee revenues from 2007–2008, 2008–2009, and 2009–2010, followed by flat or negative revenue growth in 2010–2011, 2011–2012, and 2012–2013. This excludes United in 2011–2012, which experienced an enormous jump in revenues as a result of its merger with Continental. After the shake out from the US Airways-American merger in 2013–2014, Delta, United, and American all saw positive growth in baggage fee revenues.

Figure 1: Baggage Fee Revenues for the Big 4 U.S. Carriers (2007–2014)



B. Market "Rules" Involving Distribution

The AAI encourages the DOJ to consider the effect of potential coordination among the Big 4 carriers on market "rules." Unlike naked price fixing, an agreement on rules is a more subtle form of competitive restraint whereby rivals agree on and implement practices that insulate rivals to some degree from hard competition.[34] Market rules span a variety of forms of conduct. In airlines, we draw attention, in particular, to any simultaneous or sequential adoption of strategic policies. These include, for example, attempts to impose a standardized distribution model on the industry, imposing a surcharge on itineraries purchased through any distribution channel except the airlines' own websites, or cutting off intermediaries from access to the airline data necessary to distribute airfares and products through rival distribution channels.

The AAI encourages the DOJ to take a particularly close look at policies and procedures

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[33] Jumps in baggage fee revenues for Delta from 2009–2010 and United from 2011–2012 reflect their mergers with Northwest and Continental, respectively.
[34] Robert H. Lande & Howard P. Marvel, *The Three Types of Collusion: Fixing Prices, Rivals, and Rules*, 2000 Wis. L. Rev. 941, 942–44 (2000).

promulgated and/or implemented by the International Airline Transport Association (IATA), the global airline trade association. Some of IATA's initiatives involve rivals subscribing to policies that raise concerns about potential coordinated conduct on market rules. Most recently, for example, IATA announced that:

> Working with airline members of IATA and aircraft manufacturers, an optimum size guideline for carry-on bags has been agreed that will make the best use of cabin storage space . . . A number of major international airlines have signaled their interest to join the initiative and will soon be introducing the guidelines into their operations.[35]

This particular IATA-driven policy actually failed in the face of backlash. Two U.S. Senators noted that the policy would require passengers to pay more and buy new luggage.[36] Some of the Big 4 carriers also came out against the proposal, citing investment in the "customer experience," including larger overhead bins.[37] As explained next, however, some IATA policies do gain significant traction.

1. Models of Distribution

Before exploring the foregoing strategies, consider the structure of the airline industry—and particularly the distribution segment—shown in Figure 2. The left side of the figure shows the four major components that comprise the distribution of airfares to the ultimate consumer. These are: (1) fares and schedules, (2) information infrastructure, (3) distribution channels, and (4) consumers. Figure 2 illustrates the two prevailing models of distributing air travel products and services. One is the airline model where each carrier uses its own website (e.g., United.com, Southwest.com, etc.) to sell fares and other products. These websites do not allow for comparison-shopping. The second is the third-party distribution model where various intermediaries collect, synthesize, and present data so that the consumer can engage in transparent search and comparison-shopping. The third-party distribution model features four major distribution channels: online travel agencies (OTAs) (e.g., Expedia-Orbitz, Priceline), meta search engines (e.g., Kayak, Bing, Google flight), bricks-and-mortar travel agencies, and managed travel.

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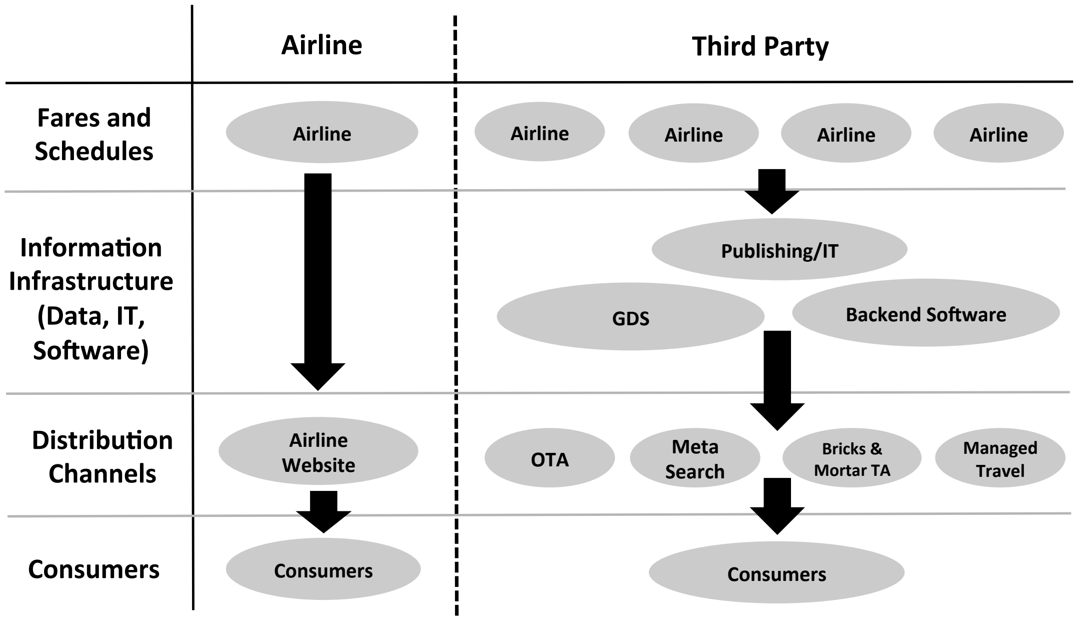
[35] Press Release, IATA, Airlines to Address Carry-On Bag Dilemma (June 9, 2015), *available at* https://www.iata.org/pressroom/pr/Pages/2015-06-09-02.aspx.

[36] *Airline group scraps plan to reduce size of carry-on luggage after backlash*, The Guardian, June 17, 2015, http://www.theguardian.com/world/2015/jun/18/airline-group-scraps-plan-to-reduce-size-of-carry-on-luggage-after-backlash.

[37] *See also Travel Tip: IATA Proposes New Dimensions for Carry-On Luggage*, Petergreenberg.com, July 2, 2015, http://petergreenberg.com/2015/07/02/iata-dimensions-for-carry-on-luggage/.

Figure 2: Models of Airfare Distribution



Competition *within* a distribution channel ("intra-channel" competition) is critical for ensuring that consumers have choice in providers within the channel they prefer. We note that technological advancements and market entry in distribution have likely created benefits for consumers. However, mergers of rivals within third party channels may be designed, in part, to enhance bargaining power to counter the market power accumulated by the airlines over the last 10 years, and increasingly exercised through their own distribution channel (i.e., airline websites).[38] Competition *between* distribution channels ("inter-channel" competition) is also vital. Different channels serve the needs of different types of consumers and provide transparency and comparative search for flights and services.

2. "Standardized" Distribution, Itinerary Surcharge Policies, and Prohibitions on Third-Party Intermediary Access to Airline Data

Airlines have moved aggressively to recapture the distribution of their own products and services, in large part because they are dissatisfied with their ability to control how consumers see information on their fares and ancillary fees. A managing director for e-commerce for a European airline recently noted, "GDSs and travel agencies that can't or won't sell our ancillary products the way we want will find that they've become invisible to us."[39] This statement reveals the root source of discontent, namely that airlines believe they have the greatest ability to sell additional products and services to consumers when they have direct access to consumer data that would allow them to dynamically price their products.

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[38] In its complaint in Google-ITA, the DOJ defined a market for "comparative flight search services," or services that enable consumers to compare information on fares and availability. DOJ found that only OTAs and meta search engines competed in the market. Beyond this distinction, the four different channels of distribution compete at some level. *See* Complaint at 7, *United States v. Google Inc.*, No. 1:11-cv-00688 (D.D.C. Oct. 5, 2011), *available at* http://www.justice.gov/file/497686/download.

[39] Henry H. Harteveldt, Atmosphere Research Grp., *The Future Of Airline Distribution: A Look Ahead To 2017*, at 11 (2012) (a special report commissioned by IATA), *available at* https://www.iata.org/whatwedo/stb/Documents/future-airline-distribution-report.pdf.

In an effort to drive the consumer toward their own distribution channel (and away from rival channels), some airlines have adopted policies that could raise anticompetitive concerns. One is the New Distribution Capability (NDC), put forward by the International Air Transport Association (IATA) in the Department of Transportation's (DOT) Resolution 787 Rulemaking.[40] IATA's Passenger Distribution Group (PDG), which endorsed the NDC standard, is made up of representatives from 11 of the largest airlines in the world.[41]

Presented as a simple proposal for a change in technical standard NDC was, for all practical purposes, an effort to create a standardized distribution model for the airline industry. NDC would fully embrace dynamic airline pricing by linking the collection of data on individual consumer characteristics to the provision of tailored information on fares and ancillary services. But standardizing distribution under a model that has been agreed to by the very rivals who compete for consumer travel dollars potentially constitutes an anticompetitive agreement on the "rules" of competition. As the AAI noted in its comments in the DOT proceeding, such an agreement on rules would soften competition between airlines *and* between an airline's own distribution channel and rival distribution channels.[42] There is nothing to prevent any individual airline from developing and unilaterally implementing dynamic pricing. There is no need, however, for the airlines to do this collectively by creating, agreeing to, and implementing a standardized distribution model for the industry.

Needless to say, the IATA NDC proposal encountered some resistance in the DOT Resolution 787 proceeding. The airlines therefore have moved forward with other strategies to capture distribution through their own channel. At the June 2015 IATA meetings in Miami, for example, Lufthansa accounced that it would impose a surcharge on all itineraries not purchased through their own dedicated websites.[43] An "informal poll of IATA members in the audience at one event, 96 of 118 respondents said their airlines might make a similar move."[44]

While the front-end surcharge strategy targets consumers to drive them toward the airline distribution channel, the airlines have also worked on the back end. An industry study notes that one of the Big 4 carriers has begun to cut off third-party intermediaries' access to information necessary to distribute flights. Delta "publicly cut off a number of different OTA and meta search sites" in December 2010. In January 2011 the airline began removing flights from CheapOAir, BookIt.com, OneTravel, CheapAir.com, Vegas.com, AirGorilla, and Globester.[45] Delta cut off a total of 21 OTAs

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[40] International Air Transport Association, Application for Approval of an Agreement (Resolution 787) by the International Air Transport Association, U.S. Dep't of Transp., Docket OST-2013-0048 (March 11, 2013) (hereinafter IATA Application).

[41] The 11 airlines are: Air Canada, Alitalia, United Airlines, Inc., Delta Air Lines Inc., Air France/KLM, British Airways p.l.c., Deutsche Lufthansa AG, Swiss International Airlines Ltd, Korean Air Lines Co. Ltd, Cathay Pacific Airways Ltd, and Singapore Airlines Ltd.

[42] *See* Am. Antitrust Inst., Comments in re: Agreement Adopted by the Passenger Services Conference of the International Air Transport Association, U.S. Dep't of Transp., Docket OST-2013-0048 (May 1, 2013), at 17, *available at* http://www.antitrustinstitute.org/sites/default/files/AAI%20Comments_OST-2013-0048.pdf.

[43] *See, e.g.*, Jack Nicas & Robert Wall, *Lufthansa Surcharge Steps Up Right for Fares*, Wall St. J., June 9, 2015, http://www.wsj.com/articles/lufthansa-surcharge-steps-up-fight-for-fares-1433894199.

[44] *Id.*

[45] Fiona Scott Morton et al., Charles River Assocs., *Benefits of Preserving Consumers' Ability to Compare Airline Fares* 26 (2015), *available at* http://www.traveltech.org/wp-content/uploads/2015/05/CRA.TravelTech.Study_.pdf. *See also* Nicolas Herst, *Airline Protest New Airline Fee*, Politico, Sept. 14, 2015, http://www.politico.eu/article/travel-agencies-complain-commission-airline-fee-lufthansa-group-ettsa/.

by mid-2011, followed in 2014 by cutting off TripAdvisor, Fly.com, Hipmunk, and Routehappy.[46]

One airline's actions alone to implement policies to restrict access to data by third party intermediaries or to impose a surcharge on itineraries booked through third party distribution channels do not necessarily raise competitive concerns. Any parallel adoption of such policies by the domestic carriers, and the effect it has on rival distribution channels and consumers, however, bears scrutiny by the DOJ, as a potential group boycott or a series of vertical agreements with anticompetitive effects.

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For all of the reasons discussed above, AAI encourages the DOJ to take a particularly wide lens in its probe to scrutinize potential collusion among the Big 4 domestic airline carriers.

Sincerely,

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[46] *Id.*