

STATEMENT OF LINDA HELLER KAMM, ACTING DEPUTY SECRETARY AND GENERAL COUNSEL OF THE DEPARTMENT OF TRANSPORTATION, BEFORE THE AVIATION SUBCOMMITTEE OF THE HOUSE PUBLIC WORKS AND TRANSPORTATION COMMITTEE, CONCERNING H.R. 5481, OCTOBER 24, 1979

Mr. Chairman and Members of the Subcommittee:

I am Linda Kamm, Acting Deputy Secretary and General Counsel of the Department of Transportation. It is a pleasure to be here today to present the Department's views on H.R. 5481, the International Air Transportation Competition Act of 1979.

I would like to compliment you, Mr. Chairman, for moving quickly to sponsor comprehensive legislation to promote the improvement and expansion of international aviation. While this is a dynamic area which has seen much progress recently, we share your belief that legislation to solidify this progress would be most useful.

In the past 18 months, we have witnessed the beginnings of a fundamental change in international aviation. During this period, the Department of Transportation has assigned a substantial amount of resources to obtaining competitively oriented bilateral agreements with our aviation trading partners. We take very seriously our responsibilities for leadership in the development of this Nation's long-term competitive international aviation policy. The interagency team that has been established through institutional arrangements among DOT, the Department of State and the CAB for the conduct of individual bilateral negotiations is working well. We believe that the success of our recent air bilateral

negotiations is ample evidence that the talents, resources and perspectives of these three agencies, have been melded effectively.

During this period, the U.S. has entered into new or significantly modified agreements with some of our major aviation partners. These agreements have been generally more procompetitive than those previously in place and thus we have seen a proliferation of new services, low-fares and strong traffic growth throughout Europe and to other areas. For example, ten U.S. cities enjoyed new direct service to Brussels, Amsterdam, or Frankfurt last summer. The continued development of this competitive environment has produced a dramatic increase in the variety of fare and service options available to the traveling public in a number of markets throughout the world.

This Administration consistently has sought and will seek bilateral agreement which provide for flexibility in pricing, routing and capacity, multiple carrier competition and liberal charter rules. The Statement of Policy for the Conduct of International Air Transportation Negotiations, issued in August of 1978, embodies these procompetitive principles. Since that statement was issued we have continued to progress towards our stated goals by concluding new or significantly modified agreements with Germany, the Netherlands, Korea, Jamaica, Belgium, Thailand and Singapore. These agreements are benefitting the traveling public by producing lower fares and additional convenient service.

For example, during the first six months of 1979, the low fares and increased service encouraged by our bilateral with Belgium produced a 100 percent increase in overall traffic, with the U.S. carrier share of the market jumping from 17 to 42 percent. The U.S.-Netherlands bilateral helped produce a 37 percent increase in traffic, with the U.S. market

rising from 13 to 17 percent. Travel to West Germany increased 24 percent with the U.S. carrier portion moving from 37 to 43 percent.

An early step in this concentrated effort to increase competition in international markets was the signing of Bermuda II, the bilateral agreement with the United Kingdom. While that agreement, from our present perspective, is less procompetitive than we would like, it provided important benefits for air service in the U.S.-U.K. market.

Today in that market there are nine U.S. and British airlines operating on a highly competitive basis. Four airlines began service within the last year. Standby, budget and apex fares, as low as 60 percent less than the standard economy fares, have been offered regularly over the past 18 months. Average summer fares between the U.S. and the U.K. have declined 14 percent at a time when carrier costs have risen significantly. Scheduled traffic in this market has skyrocketed 41 percent.

Mr. Chairman, I believe it is quite clear that our procompetitive policies, where they have been implemented, are succeeding. More people are travelling by air than ever before and they are paying significantly less for that service. U.S. carriers are responding effectively to the new environment.

We all recognize, however, that our policy cannot be implemented unilaterally in foreign markets. International aviation is based on partnerships. Many countries still remain reluctant to cast off the long tradition of close government regulation of fares and capacity and replace it with the dynamics of the marketplace.

It is the Administration's hope that the demonstrated success of increased competition which has occurred both in our domestic markets -- where the efforts of this Committee played such a pivotal role --- and in our international markets --- where U.S. policy has been implemented -- will persuade these more cautious governments to consider our proposals more favorably. We already have some indication that the demonstrated success of our policy is having an impact on these more cautious governments. Our data has shown that, as lower fares and new services have been introduced into the international marketplace over the past two years, these fares and services have "spun-off" into other markets not directly affected by a liberal agreement. For example, the New York-Paris fares have decreased eleven percent over the past two years. We will of course continue to work, along with the other interested Federal agencies, to obtain a wider acceptance of U.S. international aviation policy through the ongoing process of bilateral negotiations.

I should note, Mr. Chairman, that the airline industry is expected to earn about \$400 million in 1979, significantly less than the \$1 billion it earned in the record setting year of 1978. Some critics of airline deregulation are using the current financial decline as an argument against the effectiveness of our pro-competitive policies. It is clear, however, that the decline is due to factors which cannot reasonably be attributed to deregulation. The principal reasons for this deterioration in financial performance have been the unprecedented increase in the price of jet fuel, the grounding of the DC-10, the United Airlines strike and large investment tax credits taken by air carriers this past year. In particular, the estimated industry outlays for jet fuel have

jumped astronomically. Fuel costs now equal labor costs in the airline industry. Competitive practices cannot immunize carriers against these sorts of developments. Nevertheless, carrier financial performance under the present inflationary pressures is very good when compared to net losses sustained during such periods in the past.

We are very much aware that the scarcity of jet fuel, combined with skyrocketing fuel prices, and substantially increased pressure on the physical capacity of airports to handle increased numbers of operations and passengers have become major problems which threaten to impede further progress in domestic and international aviation. This Department and a number of other agencies have begun to examine ways in which these constraints can be alleviated. Through careful planning and with the cooperation of both carriers and airport operators, it should be possible to develop effective ways of managing our aviation resources more efficiently.

It is against this background of where we are and where we have come from that I would like to comment on H.R. 5481. The Department strongly supports most of the provisions of this bill. We are particularly supportive of those provisions which would abolish the outmoded differences between the CAB's treatment of foreign and domestic air transportation. In addition, the bill would expand the U.S. Government's range of responses to unfair or anticompetitive treatment of U.S. carriers abroad; would enable U.S. carriers in times of need to more readily increase fleet capacity through leasing without crews of foreign carrier aircraft; would provide new and positive mechanisms for action

on international fares; and would relax excessively rigid restrictions on air travel paid for with U.S. Government funds. Generally, we believe that the bill will be a positive force in the implementation of U.S. international air transportation policy and thus enhance the quality and variety of air service available to the public.

Attached to my testimony is the Department's section-by-section commentary on H.R. 5481. However, there are some provisions I would like to discuss specifically with you this morning.

#### Fare Flexibility Standards

One of the bill's most important innovations is a new section providing for a deregulated zone of reasonableness for international fares and rates. The proposed amendment is similar in concept to the fare zone that has proven successful in U.S. domestic markets. The Department supports the establishment of a zone of reasonableness for international fares. Its adoption would increase management's capability to respond to changes in the marketplace as well as to changes in carrier costs. It would reduce paperwork substantially and would be an important step towards reduction of regulatory delay. The provision thus would represent an important contribution to the achievement of U.S. international aviation policy objectives.

We have examined this provision with particular care. While the parameters of the zone --5 percent upward and 50 percent downward -- appear to be appropriate, we have some concerns about establishing October 1, 1979, fare levels as a permanent benchmark in every market. Existing international passenger fare levels in some markets may be out of line with the actual costs of operations. Some levels may be too low because of rapidly increasing fuel costs and regulatory lag. Others, particularly in less competitive markets, may be too high.

Examples of fare levels the Department believes may be too high in relation to costs are those charged in the U.S.-Caracas and U.S.-Rio markets. On a per passenger mile basis, those fare levels are 1.3 to 6.3 cents higher per mile than the standard economy fares being charged in the New York-London market. When those per mile charges are multiplied by the number of miles involved in most international air segments, the increased costs to the passenger can be substantial. To etch these fares and rates into the stone of U.S. law without a careful review of their suitability on a market-by-market basis would be unfortunate.

For this reason, we would urge that Section 24 facilitate an expedited examination of the suitability of October 1 fares as standard foreign fare levels, provide for the establishment of alternative fares in appropriate markets, and ensure an adequate opportunity for all interested parties to make known their views regarding the data and analysis upon which proposed standard foreign fare levels are based.

As to the suitability of October 1 fares, we would expect as a matter of course that any proposed departures from these historic fares in the establishment of Standard Foreign Fare Levels would be confined principally to non-competitive markets. We would hope, also, that any rulemaking proceeding instituted for the purpose of establishing alternative Standard Foreign Fare Levels be completed in six months.

We have some concern with the proposal which would require the Board to increase the Standard Foreign Fare Level at least every six months to account for the percentage change in carrier operating costs. The Board would be prohibited by the bill from making any adjustment in the costs

actually incurred. Under the present language, carriers would have a reduced incentive to hold costs down, because all cost increases incurred would be included in the next adjustment. We believe that by allowing an upward adjustment equal to some percentage of aggregate carrier costs in a given market -- 80 percent, for example -- carriers would benefit directly from their own efficiency. Such a modification in the provision would not add to the Board's administrative burden, but would avoid the economic distortions that might otherwise result from an automatic, uncritical pass-through. Where circumstances require an adjustment to the standard level beyond that provided by the 80 percent cost pass through, the Board should be authorized to make a special adjustment to the standard level.

#### Cabotage

H.R. 5481 does not address this country's long-standing policy regarding cabotage. The Department believes that cabotage should be permitted, on an emergency basis, in the event of a serious reduction of service or capacity in a U.S. domestic market.

There may be periods, for example, in which travelers holding reservations are stranded without means of alternative transportation. Under such conditions, we would favor the establishment of a mechanism for permitting foreign air carriers to alleviate any capacity shortage that might exist in the domestic system. However, such a mechanism should provide for an expedited finding that an emergency does exist based on specific criteria set forth in the statute. These emergency cabotage rights should be granted only when no other U.S. carrier capacity is available, should be limited specifically to the emergency period, and should be tailored to restore approximately the amount of capacity

that is temporarily removed from the market by the emergency circumstances. We would be pleased to work with the committee staff in drafting an amendment that preserves the availability of needed passenger-carrying capacity in a way that minimizes any adverse impact on U.S. carriers.

#### Intercarrier Agreements

The bill's proposed revision of Section 412 of the Federal Aviation Act would bring under a single regulatory regime intercarrier agreements affecting domestic air transportation and agreements affecting foreign air transportation. In our view, this is a very positive step.

Under the amendment set forth in Section 11, the filing of agreements affecting foreign air transportation would become permissive rather than mandatory as under present law. The Board would be permitted to approve an agreement which "reduces or eliminates competition" whenever it finds that the agreement is not otherwise adverse to the public interest and that it is necessary to meet a serious transportation need or to secure important public benefits, including international comity or foreign policy considerations, which cannot be achieved in a materially less anticompetitive manner. These changes would permit greater flexibility in the Board's regulatory surveillance of intercarrier agreements affecting foreign air transportation. The Department supports them.

In our view, foreign air carriers should have the same ability as U.S. carriers to initiate CAB review of these agreements. This would allow CAB review of agreements in which U.S. carriers are not participating but which affect U.S. passengers and shippers. We are pleased, therefore, to see such a provision included in this bill.

The Department would recommend one further change. Under the present statutory scheme of the Federal Aviation Act, the President is not authorized to review CAB actions regarding intercarrier agreements affecting foreign air transportation. We believe that the President should have such authority whenever the Secretary of State certifies that an intercarrier agreement has significant foreign policy implications.

We also believe that the Presidential review provision of Section 801 should be amended in one additional respect. Right now, although any Board decision affecting the terms of an operating certificate is subject to Presidential review, the grant of "exemption authority" -- allowing a carrier to serve a new market without first obtaining the certificate authority -- is not reviewable. We believe that Presidential review of such awards should be required whenever the Secretary of State certifies that significant foreign policy issues are at stake.

Mr. Chairman, I realize that the Subcommittee's time this morning is limited and I therefore have kept my remarks brief. As I stated before, I have appended to my statement a full discussion of the Department's views on each provision of H.R. 5481. I look forward to working with the Subcommittee and its staff in the weeks ahead on details of this legislation.

That completes my prepared statement. I would be pleased to answer any questions you or the members of the Subcommittee may have.