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FOR POLICY AND INTERNATIONAL AFFAIRS
BEFORE THE
AVIATION SUBCOMMITTEE
OF THE HOUSE PUBLIC WORKS AND TRANSPORTATION COMMITTEE
CONCERNING U.S. AVIATION POLICY
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Mr. Chairman, Members of the Subcommittee, I appreciate this opportunity to meet with the committee to express the administration's strong concerns regarding the four aviation bills that have been introduced in the House. The Department's main objection to these bills is that they would insert the Department in matters best left to, and currently in, the marketplace. The Department will gladly submit more specific, detailed, comments on the proposed legislation, as appropriate, once our in-depth review of the proposals is complete.

H.R. 66, 782, 2037 and 2074 address a number of areas affecting the air transportation industry, including foreign ownership interests in U.S. airlines; CRS rules and costs; the sale of gates, slots and certificates for foreign air transportation; airport gate and facility charges; and a variety of consumer-related issues pertaining to service disruptions, complaint handling, advertising, frequent flyer program rules and discount ticket conditions.

Foreign Investment

Over the past couple of years, the Department has considered a growing number of cases involving foreign investment in U.S. airlines. That investment has been in a variety of forms -- voting common stock, non-voting preferred stock, and debt. The Department has been faithful to the existing statutory requirement prohibiting foreign ownership of more than 25 percent of the voting stock of a U.S. carrier as well as to the underlying premise of ensuring that U.S. air carriers remain under the actual control of U.S. citizens.

The statutory limitation on foreign ownership interests in U.S. airlines was established at a time when commercial aviation was at an early stage of development and the world's economy was structured much more along national lines. Since then, we have seen the significant development of multinational corporations and joint ventures in many sectors of the economy and the growing importance of globalization in the air transportation industry. These developments portend a greater push for liberalization of investment restrictions with respect to the commercial air transportation industry. The recent severe economic distress in the industry and the need for additional sources of capital, particularly for carriers in weak financial condition, will also increase the pressure to relax these constraints.

Operating entirely within the bounds of existing law, the Department has substantially increased the opportunity for foreign investment in U.S. carriers while continuing to ensure actual U.S. control. In approving the KLM investment in Northwest, we allowed a higher level of foreign equity investment, in terms of total percent of equity investment by dollar amount, than had previously been permitted by the Department. The level of voting stock in that case was still below the statutory limit of 25%, and, most importantly, we were satisfied that the airline continued under the control of U.S. citizens.

As a result of those decisions, we no longer consider total foreign equity investment, by itself, to be an indicator of foreign control if it is less than 50 percent of total equity. And we no longer consider debt financing obtained from foreign sources as a potential means of control, unless the loan agreement confers extraordinary rights to the foreign lender.

Our efforts and willingness to expand investment opportunities within the existing statutory framework reflect the importance of affording our carriers the widest possible financing alternatives so that they can grow and compete effectively in the world market, as long as our vital interests, such as national security and market access, are protected.

Under our administration of the existing law, there is no problem of foreign control of U.S. airlines, and we believe that a workable program could be developed to ensure continuation of this situation while providing U.S. carriers with additional foreign investment opportunities. Therefore, the question presented is whether the law needs to be changed so as to encourage the additional flow of capital into the U.S. civil aviation industry, and if so, how we can achieve that objective while protecting our other vital interests.

Both bills contain a number of features which could form the basis for new law in this area. We are interested in the increase in the proposed level of foreign voting stock from 25 to 49%. As to the proposed conditions, which are still under review, our position is that they should not make it more difficult for U.S. airlines to obtain capital from foreign sources. This restrictive approach would inhibit domestic competition, make it more difficult for our airlines to compete with foreign carriers, and ultimately result in the loss of service for the traveling public and jobs for U.S. employees.

Computer Reservation Systems

With respect to CRSs, the proposed legislation addresses three areas.

First, one bill would prohibit vendors from discriminating against carriers in displays and forbid vendors from supplying information to any parties that would enable them to establish discriminatory displays. Second, the bills would prohibit the inclusion of certain provisions in CRS contracts between vendors and subscribers. Specifically, the bills would place constraints on the ability of vendors to impose minimum use clauses, roll contracts over at intermediate points in time, impose liquidated damage clauses, and require contracts of more than one year in length.

We have been dealing with the problem of display bias since the first CRS rules were established in the mid-1980's. We are currently reviewing our CRS rules and proposing changes that would further address this issue. On March 25, 1991, the Department issued a Notice of Proposed Rulemaking proposing to readopt the current rules stipulating that information provided be organized in an objective and unbiased manner and that participation in a CRS be open to all carriers on a non-discriminatory basis. Both our existing rules and our proposed rules go much further in defining fairness in display than the proposed legislation. As for the contract provisions, we have proposed to shorten the maximum subscription term CRS vendors can require of agents. In addition, a number of new provisions, designed to enhance competition, have been proposed. These include allowing travel agents to use equipment obtained from suppliers other than a CRS vendor and to use a single terminal for access to all CRSs. Our notice of proposed rulemaking followed extensive staff examination of the issues, the issuance of an advance notice of proposed rulemaking, and the filing and review of substantial comments by many interested parties. Comments on the Notice of Proposed Rulemaking are due June 24, with responses to comments received due in early

August. Once we have considered those comments, we will issue our final rule. We have extended our existing rule through November.

Since we are in the midst of the rulemaking process, I cannot respond to any concerns addressed to our proposed new rules. However, we are confident that our rulemaking proceeding provides the most effective forum for investigating recent developments in the CRS industry, and for taking such action as may be needed to ensure that competition remains vigorous in both the CRS industry and the air transportation industry which it affects. In these circumstances, we do not see any need for and strongly oppose new legislation in this area at this time.

Third, the proposed bills address the issue of vendor charges to participating carriers, presumably based on a concern that vendor fees are excessive. One bill proposes that arbitration procedures be established for determining participation fees when a participant objects to an increase in fees. There are both administrative and substantive problems with these proposals that make their advisability questionable. The arbitration process for setting CRS fees that has been proposed will undoubtedly be time-consuming and costly for all parties. It will require the arbitrator to determine costs and indirect revenues attributable to the CRS system, which our staff has not been able to determine with any degree of precision despite years of intensive study. Thus, we have very serious concerns about the workability of such proposals. More fundamentally, we believe that the government should not interfere with negotiations between private parties unless there is compelling evidence that the market is not functioning properly. It should be noted that our rulemaking has invited public comment on the issue of vendor fees.

<u>Asset Sales</u>

The next topic is one that has been highly visible during recent months -- the sale of gates, slots and certificates by airlines. H.R. 2037 and 2074 both address the sale of certificates for international service, while H.R. 2074 addresses the sale of gates and slots. Both of these proposed bills would require approval of such asset sales by the Secretary based on public interest and competitive findings.

Under the current regulations governing the sale of slots -- commonly referred to as the buy/sell rule -- slots may be sold or traded for any consideration and for limited or open ended periods of time. A major objective of the rule is to allow the use of the slots to be adjusted in response to market demand and, therefore, be put to their most productive use with minimal interference by the government. Since the rule took effect, transactions have occurred routinely, and it has generally worked well.

Furthermore, there are adequate safeguards to ensure that the sale of slots is not adverse to the public interest. The Department of Justice has the authority to intervene in those instances where it determines that the sale of slots would be anti-competitive. We work closely with the Justice Department when these transactions are reviewed. In that regard, I would point out that the Justice Department notified United Airlines that it would oppose its purchase of Eastern's slots and gates at Washington National Airport. Subsequently, the assets were sold to Northwest, and Justice did not oppose the transaction.

The Department also has regulatory authority to address any problems with the slot sale process. While the slot rule has generally worked well, new entrants and small incumbents have generally not succeeded in purchasing slots. The Aviation Safety and Capacity Act of 1990 requires that a rulemaking designed to improve access be initiated by July 1, 1991. Accordingly, we are currently reviewing our slot rule and expect to initiate a rulemaking in the near future.

For these reasons, the Department is strongly opposed to any legislation that involves the Department further in slot sales. The proposed statutory provisions would require the government to become much too involved in the process of slot allocations. The process would become excessively burdensome on the parties, involve the government in reaching judgments on the relative benefits to be derived from alternative uses of slots and effectively regulate schedules. The costs and problems associated with this solution are not justified.

We oppose the proposal for gate sales for similar reasons. Implementation of the proposed legislation would involve the Federal government in business dealings and contracts between local airport and municipal authorities and air carriers. The Federal government has never been involved in these dealings. It would inject the Department into the management of airports, creating additional burdens for all parties and potential delays in the allocation and utilization of available facilities. As with slot sales, the Justice Department has the authority to review the sale of gates and has blocked such a sale in the past when there were competitive problems.

As to the approval of international route transfers, we strongly oppose the proposed legislation because it would require the Department to select among competing carriers for route transfers. This is contrary to the tenets of deregulation and the objectives of the Airline Deregulation Act. Congress deregulated the airline industry because it concluded that the public would receive better service, and the airlines would operate more competitively and efficiently, if carriers were free to allocate their resources and choose their operating strategies with as little government intervention as possible.

Route sales have generally been good for the industry and the traveling public. Our review of recent experience in route transfer cases indicates that the transfers which we have approved have consistently produced net dividends for the public in terms of the real quality of service available and a net gain for the U.S. airline industry in terms of aggregate market share. In other words, the marketplace is an effective forum for allocating international route authority as long as government ensures that anti-competitive transactions are prohibited and the quality of service does not deteriorate. The Department under Secretary Skinner, working closely with the Department of Justice, has been providing this safeguard.

Although the Department of Transportation retains jurisdiction for examining the public interest considerations in international route transfers, the proposed legislation would elevate the role of the Department from determining whether a particular transfer is consistent with the public interest to determining which possible transfer would maximize the public interest. The process would become more cumbersome and costly to all parties, and would entail even more delay in the reallocation of resources to carriers that can more effectively and efficiently utilize them. We do not believe that such change is warranted or in the public interest.

Furthermore, in those instances where the public interest is not well served by a proposed route sale, the Department is able and willing to intervene. In this regard, the Department recently refused to allow TWA to transfer three of its U.S.-London routes, from St. Louis, Baltimore and Philadelphia. Likewise, last year, we refused to approve the sale of the Miami/Tampa-Toronto route from Eastern to American.

We appreciate the importance and relevance of all of the factors outlined in the proposed legislation with respect to the allocation of facilities and operating authority. Given the Secretary's on-going concerns about maintaining competition in the airline industry, as demonstrated by his undertaking of the comprehensive study on airline competition, I can assure you that he shares your objectives of maintaining a viable, competitive industry. He strongly believes, however, that the tools needed to achieve those objectives are already available, and that additional, specific legislative requirements are not necessary.

Airport Facilities

H.R. 2037 and 2074 also include proposals for improving the utilization of airport facilities by allowing peak period pricing for landing fees and by requiring airports to make unutilized gates available to carriers that have been unable to obtain access to the airport through normal market mechanisms.

The Department has been on record in favor of peak period pricing mechanisms for landing fees for a number of years. We are continuing to work with airport authorities in developing such programs within the existing statutory authority. The Department expects to publish policy guidance on peak period pricing for public comment by late summer.

As for the use of unutilized or underutilized gates, we are still analyzing this proposal. However, as I stated earlier, the proposal contained in the draft legislation would unduly interject the Federal government into business dealings and contracts between airports and air carriers. We also have strong reservations about potential administrative and procedural problems that might result from such an approach.

Consumer Protection

Two of the bills would provide consumer protection to ticket holders in the event of an airline bankruptcy. These, or similar, proposals have been submitted a number of times over the past few years. To date, the voluntary response of the industry to accommodate passengers holding tickets on a carrier that has ceased service due to bankruptcy has adequately addressed this situation. In addition, we are concerned that a mandatory, open-ended requirement to accept all such tickets could deter carriers from entering the bankrupt airline's markets, thus harming those communities and the national air transportation system, as well as inhibiting competition. Also helping to alleviate any problems in this area is the fact that most of the airline tickets now being sold are purchased with credit cards. Under Federal law consumers who purchase tickets with credit cards can obtain refunds if a carrier should cease operations. In all these circumstances, we oppose any legislation in this area since it is unnecessary and will only result in increased costs to consumers.

Finally, H.R. 2037 contains a number of other consumer provisions. We agree that air travelers should continue to receive quality air service at reasonable prices and be treated fairly by the airlines. The Department in the administration of its consumer program has taken the steps to achieve these objectives. As a result, we believe that these aspects of this bill are unnecessary and that the costs required to implement them are not justified. There may be several concepts in the bill, however, which could produce additional public benefits at reasonable cost, but we are still analyzing these subjects.

In September 1987, DOT adopted its on-time reporting rule. That same year we successfully pursued enforcement action against a number of airlines for violations of our consumer protection requirements, particularly in the areas of unrealistic scheduling, oversales, and inadequate refund procedures. Since then there have been significant changes in the quality of airline service. In addition to tracking consumer complaints and baggage problems, we now get detailed reports on the performance of almost half a million flights every month -- almost 20 million flights, to date, since the reporting rule began. The DOT Inspector General recently completed a thorough audit and found that the reported flight data were very accurate. So we have a pretty good idea of what's happening out there.

The data show that airline performance is fairly good at this point. The incentive we established in the disclosure rule seems to be working well. Approximately 80 percent of the airlines' flights now arrive on time -- compared to about 50 percent in 1986 and early 1987, before public disclosure and our enforcement investigations. And consumer complaints have dropped from 45,000 in 1987 to 24,000 in 1988, to only about 9,500 in 1990, and appear to be declining even further in number in 1991.

Only one percent of all the flights reported to DOT are cancelled for any reason other than aircraft mechanical problems. The mechanical cancellations, about two percent of scheduled flights, are clearly a matter of safety. Although there may be countless reasons for having to delay or cancel a flight, most of the non-mechanical cancellations are due to severe weather conditions, where flights safety is, of course, also an important consideration.

While there's always room for improvement, the facts on airline performance relating to consumer protection just do not support a need to impose any major new industry reporting requirements at this time. If the facts did, the Department has adequate authority to mandate such requirements through rulemaking.

We are also concerned about the financial burden that would be involved if some of the proposed requirements were adopted. For example, many of the small code-sharing airlines do not have the sophisticated computer systems needed to produce the data reports the bill envisions. And the Department's own budget does not currently allow for the creation of a large and complex new aviation data base cataloguing the many possible reasons for delays, or the staffing increases needed to handle a toll-free complaint hotline, or the establishment of a whole new set of DOT "Airport Offices" at dozens of hub airports. This would either require a large appropriation or would require the Department to take funds away from safety or capacity programs.

We are also concerned about the provision that would require that all restrictions relating to airline tickets be included in advertisements. This would effectively eliminate radio and television advertisements and make printed advertisements virtually impossible. Furthermore, DOT already requires that important restrictions be included in print advertisements and the carriers are doing so.

We also do not support the proposals for transferability of frequent flyer mileage from one carrier to another and the transferability of non-refundable and restricted tickets. We expect that the effect of these provisions would be increased costs for the carriers that would be passed along in the form of higher fares for consumers, especially higher discount fares.

I hope my general comments have been helpful. As I indicated at the beginning, we will be pleased to submit more detailed comments on the bills, if that is desired. We look forward to working with you to address these issues in the most effective way possible. I am prepared to answer any questions that you might have.