Articles

Predatory Practices & Monopolization in the Airline Industry: A Case Study of Minneapolis/St. Paul

Professor Paul Stephen Dempsey*

"In the long run, predatory pricing will reduce the number of airlines, ultimately cutting the number of flights and choices available, particularly in smaller markets. This will leave the few surviving airlines free to price just as high as they want for just as long as they want."

John Dasburg
Northwest Airlines CEO

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I. INTRODUCTION

The monopolization of air transportation is among the most pernicious of commercial events, for the price of air transport impacts the cost of doing business in entire geographic regions. At cities like Minneapolis and St. Paul, Detroit and Memphis, the suppression of competition results in a regressive wealth transfer from consumers to producers to the tune of hundreds of millions of dollars per year. It is, in effect, a hidden tax on all who must pass through the airport. Because aviation is part of the infrastructure upon which all other businesses in a community depend, excessively high air fares dampen economic activity in whole geographic regions.

For more than a decade, Northwest Airlines has been among the most aggressive carriers in responding to new entrants that dare to inaugurate service on its monopoly spokes radiating from its Fortress Hubs at Minneapolis/St. Paul [MSP], Detroit, and Memphis.[1] Numerous studies have revealed that where there are few or no low-fare carriers disciplining an incumbent monopolist, hub premiums are high and continue to increase over time. Conversely, "the greater the presence of a low-fare carrier at the hub, the lower the hub premium."[2] According to Professors Oster and Strong:

> [T]he major airlines have been able to exercise market power for extended periods at their hub aiurports. Sustained entry of low-fare carriers might threaten this market power. In these circumstances, taking steps that forego ecenomic profits in the short run in order to preserve market power in the longer run might well be rational, profit-maximizing behavior.[3]

Airports are public resources, paid for by taxpayers. To allow their monopolization, and the consumer exploitation which results from this, is antithetical to the public interest.

II. MINNEAPOLIS/ST. PAUL FARES ARE AMONG THE NATION'S HIGHEST

By the late 1990s, Northwest dominated the Minneapolis/St. Paul airport hub with an 84% share of total local and connecting enplanements; no low fare airline accounted for more than a 2% market share. At the hubs it dominates, Northwest Airlines has achieved the highest level of seat capacity (78.3%) and gate domination (73.4%) of any major U.S.

1. *See* Lisa Zagaroli, *Northwest Plays Tough To Lock In Fares at Metro*, DETRIOT NEWS, July 20, 2000.

2. *See* e.g., CLINTON OSTER, JR. & JOHN STRONG, PREDATORY PRACTICES IN THE U.S. AIRLINE INDUSTRY (College of William and Mary Jan. 15, 2001), *available at* http://ostpxweb.dot.gov/aviation/domestic-competition/predpractices.pdf.

3. Oster, supra note 2.

airline at their corresponding hubs.[4] Northwest has gained a near monopoly position in a majority of the city-pair markets served by the MSP airport. Monopoly is usually accompanied by high prices, little consumer choice, and poor service quality.

Northwest has used its entrenched monopoly power to impose high fares in the markets served to and from the MSP airport. Numerous studies have documented the impact of Northwest's monopoly power at MSP. For example, by the third quarter of 1998, travelers using MSP airport were paying the third highest fares in the nation. High fares damage the communities served (1) by transferring wealth to Northwest and (2) by dramatically reducing trips taken by discretionary travelers. Because of Northwest's high fares there have been fewer vacation trips, fewer trips to see friends and relatives, and fewer trips by price sensitive business travelers. By reducing consumer choices, high fares adversely affect the quality of life of all who are deterred from traveling.

The table below reveals the extent to which air travel has been suppressed in the MSP market. As an economic region, the Minneapolis/St. Paul area is the thirteenth largest market in the US – larger than other metropolitan areas with substantial hub operations such as Phoenix, Denver or St. Louis. Each of these cities, except Minneapolis/St. Paul, plays home to both a large hub carrier *and* a low fare alternative. And each city has significantly more air travelers than Minneapolis/St. Paul: Denver, with a population 19% lower than Minneapolis/St. Paul has 33% more origin and destination passengers; Phoenix, with a population 7% lower than Minneapolis/St. Paul has 59% more origin and destination passengers; Atlanta, with a population only 16% greater than Minneapolis/St. Paul has more than double the number of local origin and destination passengers, and roughly twice the number of daily departures.

In the airline industry, market share appears to be strongly correlated with prices. Higher market shares ordinarily translate into higher prices; where competition erodes market share, the converse is true as well. Average fares at some of these airports can be 50 to 60 percent higher when compared to more competitive markets.[5]

4. BRIAN HARRIS, 2000 HUB FACTBOOK 33, 40 (Salomon Smith Barney 2000).

5. Northwest insists it is not a monopolist because it accounts for only 60% of MSP origin-and-destination [O&D] traffic. SEE NORTHWEST AIRLINES, THE DEMPSEY REPORT ON NORTHWEST: WRONG ON THE FACTS; WRONG ON THE LAW AND WRONG ON COMPETITION POLICY (November 2000) (hereinafter NORTHWEST REBUTTAL). However, the above chart concedes that Northwest accounts for a MSP O&D market share somewhere between 61-68% during the 1990s. The above charts also reveal that Northwest accounts for more than 80% of total traffic at MSP. To be a monopolist does not require control of 100% of the market. Moreover, if one excludes the "live and let live" oligopoly markets in which other major carriers serve MSP from their hubs (e.g., Newark, Chicago O'Hare, Cleveland, Philadelphia, Pittsburgh and Atlanta), Northwest's origin-and-destination share at MSP

MINNEAPOLIS/ST. PAUL AIR TRAVEL IS SUPPRESSED BY HIGH AIR FARES

TOP 25 ORIGIN/DESTINATION MARKETS IN THE US – 1999

Rank	Market	Passengers*	Population*	Income Rank
1	Los Angeles	51.9	16.1	2
2	New York	51.5	19.2	1
3	Chicago	37.5	9.0	3
4	Washington DC	35.0	5.4	7
5	San Francisco—Oakland	29.0	6.7	5
6	Atlanta	26.0	4.7	12
7	Dallas/Ft. Worth	25.2	5.4	8
8	Las Vegas	23.8		
9	Orlando	22.0	2.8	20
10	Miami—Ft. Lauderdale	21.6	3.8	14
11	Phoenix	20.3	3.7	17
12	Boston	19.4	5.9	6
13	Seattle	18.4	4.1	11
14	Houston	17.2	4.8	10
15	Denver	17.0	3.2	16
16	Detroit	14.8	5.0	9
17	San Diego	13.6	2.9	19
18	Tampa	13.4	3.6	15
19	Philadelphia	12.9	7.3	4
20	Minneapolis/St. Paul	12.7	3.9	13
21	Honolulu	12.2		
22	St. Louis	10.6	3.0	18
23	Portland	10.4	2.6	21
24	San Jose	10.3		
25	Kansas City	9.5	2.1	22
	* *millions*			

The U.S. General Accounting Office [GAO], the investigative arm of the U.S. Congress, has issued numerous studies of the impact of airline deregulation. The most comprehensive studies of the effect of airport concentration upon pricing are those performed by the GAO. In comparing prices at 15 concentrated hub airports[6] and 38 relatively unconcentrated airports, the GAO found that prices were 27% higher in the concentrated hubs.[7] A decade after deregulation, prices per mile charged

was 77% for the year ending December 1999. Before Sun Country's entry, Northwest had no competition on a dozen of its busiest routes.

6. Concentrated airports were those defined as having more than 60% of enplanements handled by a single airline. *See* UNITED STATES DEP'T OF TRANSPORTATION, COMPETITION IN THE U.S. DOMESTIC AIRLINE INDUSTRY: THE NEED FOR A POLICY TO PREVENT UNFAIR PRCTICES (May 1999).

7. U.S. GENERAL ACCOUNTING OFFICE, AIRLINE COMPETITION 2, 3 (1989). The report was subsequently updated and expanded. *See* U.S. GENERAL ACCOUNTING OFFICE, AIRLINE COMPETITION (1990); PAUL STEPHEN DEMPSEY, FLYING BLIND: THE FAILURE OF AIRLINE DEREGULATION 18-19 (1990). ("The higher fares at concentrated airports do not reflect a premium for non-stop service, since the average number of coupons per traveler at concentrated airports

by dominant airlines at concentrated hubs were 38% higher than those charged at unconcentrated airports.[8]

The U.S. Department of Transportation [DOT] also studied the impact of concentration on airline pricing, and concluded:

> The average fare per mile at the eight most concentrated hubs is higher than the national average. Adjusting for the average trip distance and the size of the market served at the eight most concentrated hubs, fares were on average 18.7% higher than similar markets for other airports. This finding supports the conclusion that high hub concentration leads to high fares for passengers traveling to and from such cities.[9]

More recently, the DOT found that, "In the absence of competition, the major carrier is able to charge fares that exceed its fares in non-hub markets of comparable distance and density by upwards of 40 percent."[10]

Though in another study the GAO found that air fares had fallen since deregulation at most airports serving communities of all sizes, it reported that fares at Minneapolis increased 17.4% between 1979 (just after deregulation) and 1994 – the second-highest percentage increase of any of the 25 large-community airports it surveyed.[11]

Another study revealed that concentration at the Minneapolis/St. Paul hub caused a 72% increase in prices from 1988 to 1995, and that by 1995, its residents were paying ticket prices aggregating $693 million above the national average.[12]

By 1996, the U.S. Department of Transportation [DOT] had found that Northwest was the nation's most expensive airline, particularly on

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was virtually identical to that at the comparison, unconcentrated airports (2.26 vs. 2.28 coupons). And the difference persisted when average trip length was controlled for, by excluding from the comparison group of airports those where average trip length was significantly longer than for concentrated airports. Thus neither a higher proportion of non-stops nor a higher proportion of short haul (and thus more costly) flights can explain the fare premium at concentrated airports. The study also found that the increase in fares was generally greater at concentrated airports, and that the increase in fares was especially dramatic when a carrier established dominance during the period. . .[f]inally, the study found that in 13 of the 14 concentrated airports, the dominant carrier had higher fares, in some cases very much higher than other carriers at the same airport").

8. U.S. General Accounting Office, *supra* note 7 at 3.

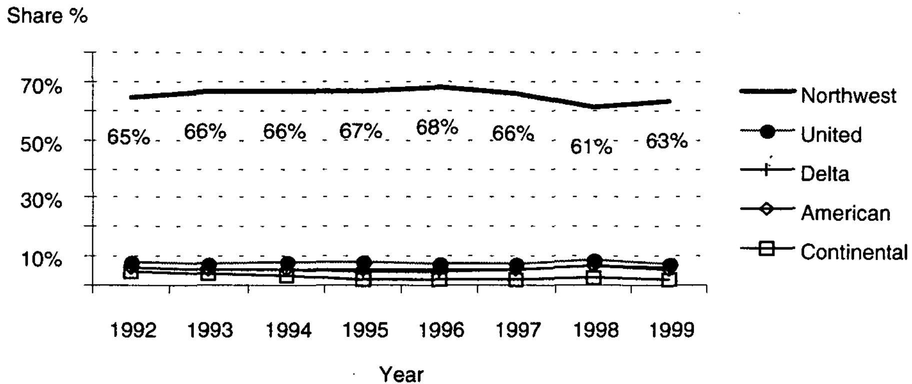
9. U.S. Dep't of Transportation, Secretary's Task Force On Competition In The U.S. Domestic Airline Industry, Executive Summary 8 (1990).

10. U.S. Dep't of Transportation, Enforcement Policy Regarding Unfair Exclusionary Conduct in the Air Transportation Indutry, 63 Fed. Reg. 17919 (April 10, 1998).

11. U.S. General Accounting Office, Airline Deregulation: Changes in Air Fares, Service, and Safety at Small, Medium-Sized and Large Communities GAO/ RCED-96-79 66-67(Apr. 1996) (showing graphically how only Pittsburgh had a higher percentage increase than Minneapolis).

12. Mike Meyers, *Minnesotans Indeed Pay More For Air Fare, DOT Says*, MINNEAPOLIS STAR TRIBUNE, Apr. 25, 1996, at 1A.

NORTHWEST SHARE OF MINNEAPOLIS/ST. PAUL ORIGIN AND DESTINATION TRAFFIC



Source: US Department of Transportation; Passenger Origin-Destination Survey

flights of less than 750 miles.[13]

By the third quarter of 1998, average fares at Minneapolis/St. Paul were the third highest in the nation. Of eighty cities studied by the DOT, Minneapolis/St. Paul passengers paid $65 more one-way, or 38% above, the average. Only two other major cities – Cincinnati and Charlotte, both hub airports as well – had higher fares. Fares in Memphis, where Northwest also maintains a hub, were tenth highest of the cities studied.[14]

In 1999, the GAO reported that average fares at Minneapolis/St. Paul were 49% higher than the national average for trips of comparable distances, up from 45% in 1995.[15] Reviewing the study, Minnesota state economist Tom Stinson said, "it makes you less competitive in the national economy and less competitive in the global economy." The GAO study also revealed that Northwest-dominated Duluth, Minn., and Fargo, N.D., were two of only three cities in the nation where inflation-adjusted fares increased from 1990 to 1998. Consumers at Northwest's Detroit hub paid a 20% fare premium.[16] In January 2001, the U.S. Department of Transportation reported that Minneapolis/St. Paul consumers paid a hub premium of 55%—the third highest in the nation – while consumers at Memphis paid a 43% hub premium, and Detroit paid a 40% hub

13. Mike Brenner, Dan Fricker & Garry Volgenau, *U.S. Is Looking at Fares at NWA*, DETROIT FREE PRESS, Feb. 27, 1998.

14. Greg Gordon, *Federal Study Concludes Twin Cities Air Travelers Pay High Premium*, MINNEAPOLIS STAR TRIBUNE, May 1, 1999, at 1D.

15. MINNESOTA PLANNING, FLIGHT PLAN: AIRLINE COMPETITION IN MINNESOTA (1999) *available at* http://www.mnplan.state.mn.us/Report.html.

16. Mike Myers, *Air Fares Still High In Cities Despite Drop*, MINNEAPOLIS STAR TRIBUNE, Mar. 5, 1999, at 1A.

premium.[17]

The Transportation Research Board found that, "For nearly two decades now, the literature consistently has shown higher fares in city pair markets that include a concentrated hub as either the origin or destination point; this especially applies to short-haul markets in which one or two hubbing carriers handle most of the local traffic."[18] The U.S. Department of Transportation has found, "A hub airline faces only limited competition in most of its nonstop hub markets, although connecting service in long haul markets provides some discipline for the non-stop fares. As a matter of economic theory, a firm will ordinarily charge supracompetitive prices when it has no competition."[19]

STUDIES FIND HIGHER FARES AT MINNEAPOLIS-ST. PAUL

Year	Comparison	Fares at Minneapolis-St Paul
1998	9 gate-constrained and 36 non gate-constrained airports	Overall fares were 49% over average
	(US General Accounting Office, 1999)	
1996	30 busiest U.S. airports	Northwest 34% over average
	(Severin Borenstein, 1996)	
1995	60 large and medium airport	Overall fares were 41% over average
	(US Department of Transportation)	
1992	Concentrated and unconcentrated airports	Overall fares were 30% over average
	(US General Accounting Office, 1993)	

Source: Minnesota Planning Commission; "Flight Plan: Airline Competition in Minnesota

But according to Northwest Vice President Elliot Seiden, "the available evidence does not support the allegation that network airlines extract a 'hub premium'."[20] Northwest financed a study to prove that there was no hub premium, a conclusion reached by no independent study since deregulation.[21] The study was produced by Professors Darryl Jenkins and Robert Gordon. Contrary to nearly all prior research on the subject, they described the "hub premium" as a "myth." The Northwest

17. U.S. DEP'T OF TRANSPORTATION, DOMINATED HUB FARES (January 2001) *available at* http://ostpxweb.dot.gov/aviation/domestic-competition/hubpaper.pdf (data is for year end 1999).

18. TRANSPORTATION RESEARCH BOARD, ENTRY AND COMPETITION IN THE U.S. AIRLINE INDUSTRY: ISSUES AND OPPORTUNITIES 72 (1999).

19. U.S. DEP'T OF TRANSPORTATION, supra note 17; U.S. DEP'T OF TRANSPORTATION, ENFORCEMENT POLICY REGARDING UNFAIR EXCLUSIONARY CONDUCT IN THE AIR TRANSPORTATION INDUSTRY, Docket OST-98-3713 (Jan. 17, 2001).

20. *State of Competition in the Airline Industry: Oversight Hearing Before the House Judiciary Comm.*, 105th Congr. (May 19, 1998) (prepared statement of Elliott M. Seiden, Vice President, Law and Government Affairs).

21. *Id.* (contending additionally that Northwest's acquisition of Continental Airlines would not reduce competition).

Airlines' study insisted that, instead of higher fares, "residents of Minneapolis/St. Paul, Detroit and Memphis actually enjoyed a modest hub discount of 4 percent . . . ." Furthermore, Jenkins and Gordon concluded, "Those passengers originating or terminating their travel in a Northwest hub receive a travel bargain compared to other passengers on Northwest Airlines."[22]

The Jenkins-Gordon study was quickly and widely criticized. Frank Berardino, President of Gellman Research Associates observed, "Only Northwest Airlines' fares are included in the analysis, and so, the full competitive alternatives available to consumers are never part of the comparison. Therefore, how do we know if the fares are relatively high or low? . . . The authors never report their regression analysis; their whole hub premium comparison is based on them." Noting that the Jenkins-Gordon study failed to compare fares at dominated and non-dominated hubs, Kevin Mitchell of the Business Travel Coalition concluded, "the study's results fly like arrows thick and fast at the conclusion of virtually every credible analysis regarding hub premiums since deregulation . . . ."[23] Five major independent studies of airline pricing at Minneapolis/St. Paul since 1990 have concluded that fares are between 30% and 49% higher for trips beginning or ending at MSP than in competitive markets.[24]

In January 2001, the U.S. Department of Transportation issued a study on "Dominated Hub Fares". On its first page, the DOT sharply criticized the Jenkins-Gordan study:

> [O]thers have reported on the prevalence of high fares paid by passengers at hub airports dominated by a network carrier; indeed, no credible study concludes otherwise. . . . A hub study prepared by Professors Darryl Jenkins and Robert Gordon and funded by Northwest, "Hub and Network Pricing in the Northwest Airlines Domestic System," purports to show that Northwest fares in its nonstop hub markets are lower than Northwest fares in competitive connecting markets. Aside from finding the study's conclusion implausible, we have been unable to determine how the authors reached their result. The authors have not responded to our requests for further detail about the analytical model used.[25]

22. DARRYL JENKINS & ROBERT GORDON, HUB AND NETWORK PRICING (2000). Northwest Airlines argues that the Jenkins/Gordan study proves significant hub premiums do not exist. Hub airports have large numbers of business travelers who purchase unrestricted fares. *See* NORTHWEST REBUTTAL, supra note 5. But not even the DOT takes that study seriously. In attempting to determine average fares, it is inappropriate to disaggregate business from leisure fares. The average price is the average price. That business travelers are taking a price beating reflects the strength of the monopoly premium. Business travelers have only one dominant choice to all business destinations.

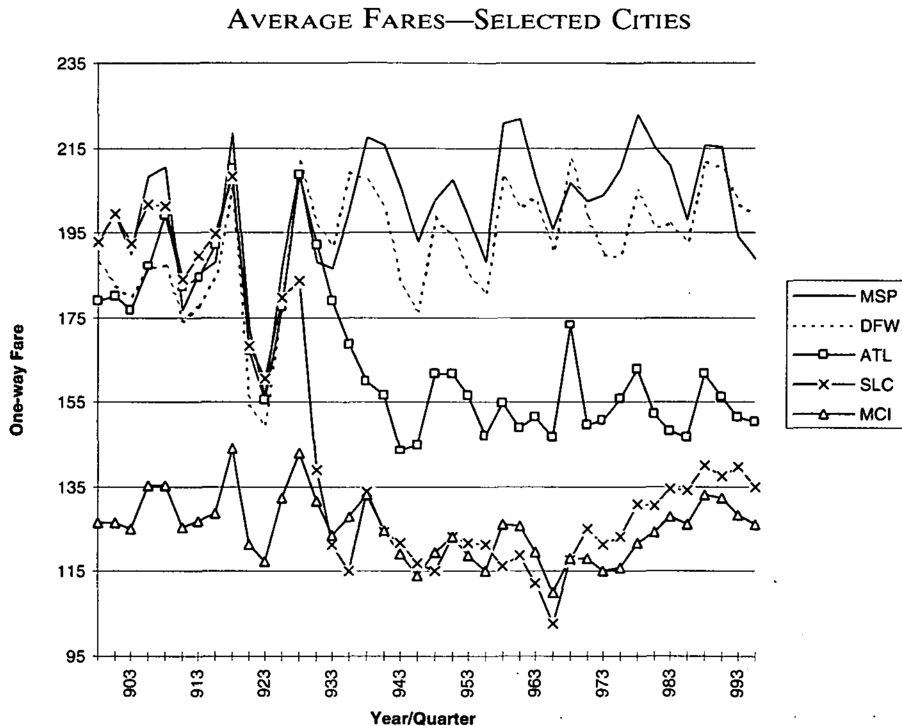
23. Letter to the Editor by Kevin P. Mitchell, BUS. TRAVEL NEWS, Oct. 15, 1999.

24. MINNESOTA PLANNING, *supra* note 15.

25. U.S. DEP'T OF TRANSPORTATION, *supra* note 17.

As described earlier, concentration levels often correlate with price levels—higher concentration tends to equate to higher prices in many markets. But the identity of the competitor can also have a significant influence on pricing. The presence of a low-cost/low fare competitor (such as Southwest, AirTran, Vanguard, Spirit, Jet Blue, or Sun Country, for example) can result in significant competitive discipline and consumer savings. According to the DOT, fares tend to be $80 higher on average when no low-fare competitor is present on the route.[26] This is reflected in the chart which shows historical average one-way fares at five airports—Minneapolis/St. Paul, Dallas/Ft. Worth, Atlanta, Salt Lake City, and Kansas City.

AVERAGE FARES—SELECTED CITIES



Source: US Department of Transportation, Passenger Origin - Destination Survey.
Note: Decline in Minneapolis/St. Paul fares in the third quarter of 1999 correlates with the initiation of scheduled service by Sun Country.

At various times, Braniff, Eastern and TWA attempted to establish a hub at Kansas City. Each failed. The result is that Kansas City remains

26. DOT Assistant Secretary Patrick Murphy, Address before the ABA Forum on Air & Space Law (San Francisco, CA, July 8, 1998).

unconcentrated (Southwest is the largest carrier, with 23% of enplanements), and consumers there enjoy average fares among the lowest of any city its size. Note that average fares at Salt Lake City and Atlanta marched in "lock-step" with fares at Minneapolis/St. Paul, Dallas/Ft. Worth and Washington/Dulles until 1994. In that year, Southwest acquired Salt Lake City-based Morris Air. Average fares dropped by 50% in Southwest's markets, while traffic tripled. By late 1995, average fares in markets served by Southwest were only one-third the level of fares in other Salt Lake City markets.[27] By 1996, Southwest accounted for 12% of enplanements, and Salt Lake City's average fares were as low as Kansas City's. At Atlanta, ValuJet's entry has brought fares down, though it only accounted for 8% of enplanements.

Contrast these price declines with the relatively higher prices at Dallas/Ft. Worth and Minneapolis/St. Paul. Dallas/Ft. Worth International Airport is dominated by two megacarriers—American (65%) and Delta (19%). Prices are somewhat disciplined in the short-haul market departing from this area due to the presence of Southwest at Dallas Love Field. Minneapolis/St. Paul suffers far more exorbitant airfares, as reflected in the foregoing chart. Northwest dominated the hub, accounting for between a 74%-85% share of local and connecting enplanements, with no low-cost/low-fare carrier accounting for even a 1% market share, and no secondary airport in the area.[28] In fact, average round-trip fares at Minneapolis from the first quarter of 1994 through the second quarter of 1999 of $416 are 43% higher than at Atlanta (where the average fare was about $252 round trip), 68% higher than at Salt Lake City (where the average fare during this period was $248), and 70% higher than at Kansas City (where the average round-trip fare was $244).

One study estimated that higher-than-average fares cost Minneapolis travelers some $500 million per year.[29] Actually, if Minneapolis/St. Paul fares were set at the level of fares in Atlanta (where AirTran maintains about an 8% market share), MSP's 12-million origin-and-destination (O&D) passengers would be saving several hundred million dollars per year. If MSP's fares were set at the level of those prevailing in Salt Lake City (where Southwest maintains about an 11% market share), or at unconcentrated Kansas City, MSP's 12-million O&D passengers would be saving even more. As the Minnesota Planning Commission identified in a 1999 report, concentration, not the hub, is the main issue. Professors Oster and Strong note, "[b]ecause the presence of the low-fare carrier has

27. Testimony of DOT Assistant Secretary Patrick Murphy Before the U.S. Senate Appropriations Subcommittee (May 5, 1998).

28. Julius Maldutis, *Airline Competition at the 50 Largest U.S. Airports—Update* Salomon Bros., (July 23, 1997).

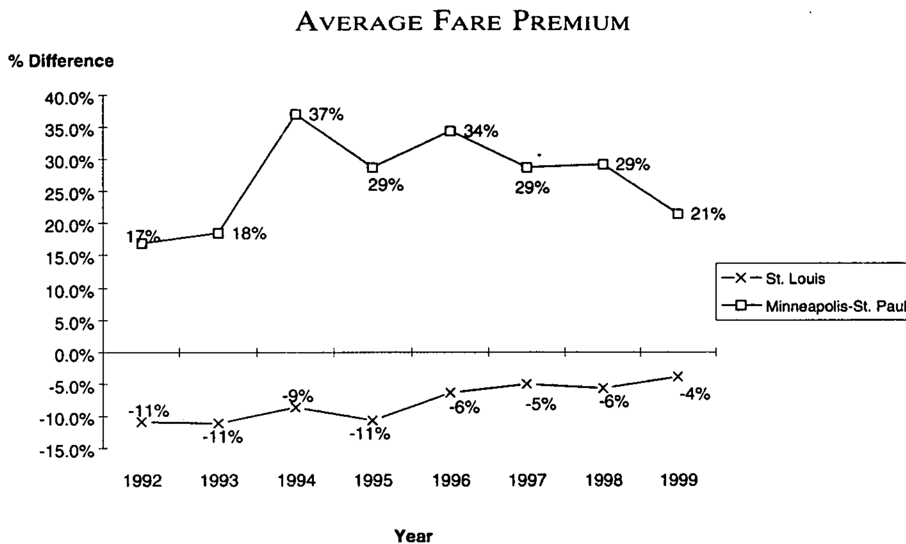
29. MINNESOTA PLANNING, *supra* note 15.

such a dramatic effect on hub premiums, predatory practices are especially likely to be targeted at low-fare new entrants."[30]

St. Louis Enjoys Hub Status With Lower Fares

Northwest passengers in Minneapolis/St. Paul pay much higher fares for hub service than TWA passengers in St. Louis, where Southwest Airlines competes for traffic. Both airports are similar in size, with a central US location.

AVERAGE FARE PREMIUM



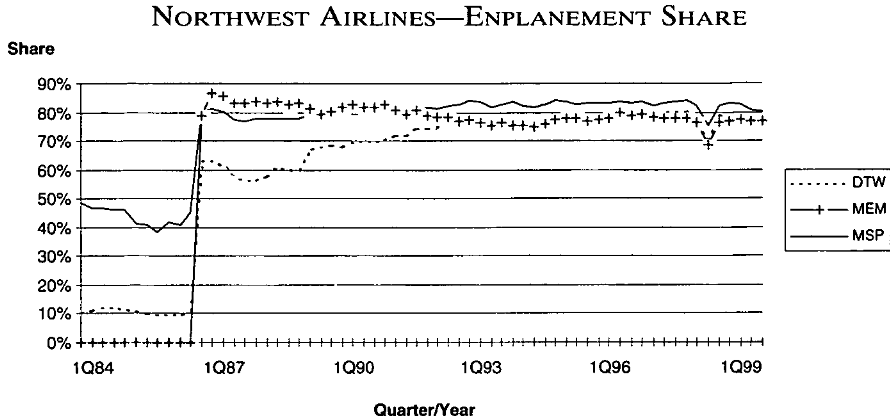
III. NORTHWEST ACQUIRES REPUBLIC AIRLINES

To expand quickly, and to monopolize major airports, some carriers have digested rival airlines. Domestic entry and ratemaking jurisdiction was phased out by the Airline Deregulation Act; but authority over mergers, consolidations and acquisitions was transferred to the U.S. Department of Transportation [DOT] on January 1, 1985. The DOT's highly permissive policies with respect to mergers led to an explosion of such activity. The DOT approved each of the twenty-one mergers and acquisitions submitted to it, including the following: American-Air Cal; United-Pan Am (various route systems); Delta-Western; Continental-PeopleExpress-Frontier-Eastern; USAir-Piedmont; TWA-Ozark; Southwest-Muse; and Northwest-Republic. Many of these mergers were approved under

30. Oster, *supra* note 2.

the then-prevailing (and since discredited)[31] neo-classical economics view that "contestability" of markets would arrest any anticompetitive conduct.[32]

NORTHWEST AIRLINES—ENPLANEMENT SHARE



Source: US Department of Transportation; T-100 Monthly Operating Statistics by Carrier Entity

The Northwest-Republic and TWA-Ozark mergers were vigorously opposed by the U.S. Department of Justice [DOJ] on grounds that they would create hub monopolies at Minneapolis and St. Louis, respectively. In the Northwest-Republic merger, the Justice Department argued that the merger would result in a reduction of competition in 42 markets, all but four of which radiated from the carriers' common hubs at Minneapolis (26 cities) and Detroit (12 cities). In 29 additional city-pair markets, the combined carrier would have 80% of the existing capacity. DOJ pointed out the extreme northerly location of Minneapolis/St. Paul made it an unlikely candidate as a hub for a new entrant.[33] But at the time DOJ participated in an advisory capacity only, and again, DOT approved all mergers submitted to it (although a few were conditioned on a spin-off of certain routes and slots). Nonetheless, the DOT approved the Northwest-Republic merger on August 12, 1986.

In 1986, Northwest and Republic Airlines were the nation's eighth and ninth largest carriers, respectively, and held the largest market shares at Minneapolis/St. Paul, Detroit, and Memphis. That year, Northwest ac-

31. *See* PAUL DEMPSEY & LAURENCE GESELL, AIRLINE MANAGEMENT: STRATEGIES FOR THE 21ST CENTURY 69-84 (Coast Aire 1997).

32. PAUL DEMPSEY, THE SOCIAL & ECONOMIC CONSEQUENCES OF DEREGULATION131-47 (1989).

33. Paul Dempsey, *Antitrust Law & Policy in Transportation: Monopoly Is the Name of the Game*, 21 Ga. L. Rev. 505, 537-38 (1987).

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quired Republic for $884 million. Republic itself was a product of the 1979 merger of North Central, Southern and Hughes Airwest.

As the above chart reveals, Northwest Airline's passenger market shares doubled after its 1986 acquisition of Republic Airlines, a carrier which until then accounted for about a third of the Minneapolis/St. Paul market.[34] A 1988 study compared fares in markets radiating from Minneapolis-St. Paul in which Northwest and Republic Airlines competed prior to their merger, and found that after the merger prices rose between 18%-40%.[35]

According to Alfred Kahn, "Spotty antitrust enforcement in the first place may be a reason there's so much concentration in Minnesota and other markets. Surely we should have ensured that the antitrust laws were reinforced when Northwest merged with Republic."[36]

A 1997 antitrust suit alleging that Northwest Airlines violated the antitrust laws by engaging in predatory behavior following its 1986 acquisition of Republic Airlines was reinstated in February 1999.[37] The suit alleges Northwest overcharged consumers as much as $400 million.[38] Plaintiffs ask that Northwest be restrained from engaging in anticompetitive conduct.[39] Specifically, plaintiffs allege:

> Numerous studies have documented the ability of airlines with dominant market shares at "fortress hubs" to discourage and defeat new entry by the use of exclusionary marketing and pricing policies. Northwest has pursued exclusionary pricing and marketing strategies that are unremunerative for Northwest but for their effect of defeating and deterring new entry. Northwest has communicated to new entrants, by public statements and by its conduct that Northwest will pursue vigorously its announced strategy with respect to new entrants at [Minneapolis/St. Paul]. This strategy has succeeded in deterring and defeating new entry by raising the non-recoverable costs of entry.[40]

34. U.S. DEP'T OF TRANSP., T-100 MONTHLY OPERATING STATISTICS BY CARRIER ENTITY (These data are based on passenger enplanements).

35. Tom Hamburger, *Fares Rose With NWA's Dominance*, MINNEAPOLIS STAR TRIBUNE, Dec. 23, 1988, at 1A. ("In 15 of the 18 hubs in which a single carrier controls more than 50% of the market, passengers pay significantly more than the industry norm").

36. Mike Hughlett, *Northwest Airlines Strike Points Up Concentration of Aviation*, ST. PAUL PIONEER PRESS, Sept. 12, 1998.

37. *See* Midwestern Machinery, Inc. v. Northwest Airlines, Inc., 167 F.3d 439 (8th Cir. 1999).

38. Kelley Holland, *Minnesotans vs. Northwest*, BUS. WEEK, Feb. 15, 1999, at 44. ("These are not the first plaintiffs to allege the Northwest's acquisition of Republic was an attempt to create a monopoly"). *See also* Fischer v. NWA, Inc., 883 F.2d 594 (8th Cir. 1989) (holding plaintiffs failed to establish an antitrust injury).

39. Tony Kennedy, *Northwest sued over alleged fare overcharges*, MINNEAPOLIS STAR TRIBUNE, June 17, 1997, at 01A.

40. *Midwestern Machinery, Inc. v. Northwest Airlines, Inc.*, 990 F. Supp. 1128, 1130 (D. Minn. 1998).

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The acquisition of Republic gave Northwest significant domestic feed for its international routes, and undisputed control of the hubs of Minneapolis/St. Paul, Detroit, and Memphis. But it also forced management to put together fourteen union groups, several incompatible fleets, and corporate cultures. Service levels deteriorated due to the clash of corporate cultures, procedures and equipment. As one response, in 1991 Northwest inaugurated its "Northbest" University training program for its customer service personnel in an attempt to overcome its "Northworst" service reputation.[41]

More recently, Northwest acquired (and has since divested) a controlling interest in Continental Airlines. Citing several major routes on which the combined carriers would have a monopoly, the U.S. Justice Department filed suit to block the acquisition, alleging, "As a result of Northwest's acquisition of control of Continental, consumers likely will pay higher prices and receive lower quality service for scheduled airline passenger service in the markets dominated by Northwest and Continental, and lose the benefit of new, competitive entry by Continental against Northwest."[42] The following table reveals the combined market shares of the merged airlines in several important city pairs.

NORTHWEST/CONTINENTAL HUB-TO-HUB NONSTOP SHARES			
Route	NW Share	CO Share	Combined NW & CO Share
Detroit-Cleveland	73%	19%	92%
Detroit-New York	75%	17%	92%
Detroit-Houston	48%	52%	100%
Memphis-Houston	39%	61%	100%
Minneapolis-Cleveland	75%	25%	100%
Minneapolis-New York	79%	17%	96%
Minneapolis-Houston	58%	38%	96%

Source: US Department of Transportation; Passenger Origin-Destination Survey.

IV. NORTHWEST FALLS TO A LEVERAGED BUY-OUT

Northwest's tenacious efforts to suppress competition so as to maintain its monopoly fares may be motivated by the unfortunate financial condition in which it was placed as a result of a leveraged buy-out of the company in 1989. Maintaining prices at supra-competitive levels enables it to pay down balance sheet debt. Certainly, its poor financial condition

41. MORGAN STANLEY, NORTHWEST AIRLINES (Oct. 31, 1994), at 2.
42. MINNESOTA PLANNING, *supra* note 15.

played a role in leading it to seek a taxpayer-funded bail out from the citizens of Minnesota.

A. The Corporate Raiders Circle

Northwest entered deregulation with perhaps the strongest balance sheet in the industry. Unfortunately, this would make it a prime candidate for LBO, which turned one of the industry's strongest balance sheets into one of the weakest.

Owned aircraft have large residual values. In 1970, Northwest's Don Nyrop began selling off his fleet of 707s (then about 12 years old, on average), and used the proceeds to purchase new aircraft, particularly DC-10s. Between 1971 and 1978, these proceeds from the sale of old aircraft provided more than a third of the total capital cost of the purchase of new aircraft. During this period, nearly a third of Northwest's pre-tax earnings came from these sales.[43] A sale/leaseback results in an immediate capitalization of these values on a discounted basis with a loss of these long-term residual values. In other words, the short-term benefits of leasing results in a sacrifice of the long-term values of aircraft ownership.

Unfortunately, low debt has subjected some airlines to leveraged buy outs. Low debt suggests that there are lots of assets owned which can be sold to pay off the debt assumed during the acquisition. For example, Northwest had one of the lowest percentages of aircraft leased (4%) and one of the industry's cleanest balance sheets prior to its acquisition of Republic in 1986.[44] Before 1990, Northwest had been consistently profitable every year since 1949.[45] Until then, Northwest had produced 39 straight years of profitability, a record no other U.S. carrier could match.[46] Among major airlines, only Delta had a more favorable debt-to-equity ratio.[47]

Denver oil king Marvin Davis began a hostile takeover bid for Northwest Airlines in 1989, offering $2.7 billion. He was out-bid by Alfred Checchi and associates, offering $3.7 billion.[48] The transaction increased Northwest's debt-to-equity ratio from 0.42/1 to 5.85/1, allowing Wings Holdings, Inc., to acquire control of Northwest with 81.5% debt and 18.5% equity. Wings' debt was $3.1 billion, almost two-thirds of

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43. ESG Aviation Services, 8 The Airline Monitor (Feb. 1996).

44. Aviation Daily, November 6, 1986.

45. Paul Dempsey & Andrew Goetz, Airline Deregulation & Laissez Faire Mythology 132 (Quorum 1992).

46. Smith Barney, Northwest Airlines Corp. (Sept. 8, 1994).

47. Transportation Research Board, Winds of Change: Domestic Air Transport Since Deregulation 72 (1991).

48. Dempsey, *supra* note 45 at 14.

which was put up by Japanese banks. Equity was $705 million, of which Alfred Checchi, Gary Wilson and Frederick Malek put up only $40 million (for which they received about half the voting and nonvoting common stock), KLM (a Netherlands airline) put up $400 million (or 57% of the equity, for which KLM received 70% of Wings' nonvoting preferred stock, 31% of its nonvoting common stock, and 4.9% of its voting common stock, as well as a warrant allowing it to convert up to $50 million of its preferred stock into common stock, some of which could be voting), and Elders IXL (an Australian company) put up $80 million (or 11% of the equity, for which it received 10% of Wings' nonvoting preferred stock, 16% of its nonvoting common stock, and 15.4% of its voting stock).[49]

Wings, which became the parent company of Northwest, encumbered Northwest's balance sheet with several billion dollars of debt as a result of the LBO. That is more than the purchase price of Pan Am's trans-Pacific division (bought by United for $715 million), Western Airlines (bought by Delta for $860 million), Ozark Airlines (bought by TWA for $250 million), Eastern Airlines and People Express (bought by Texas Air for $676 million and $112 million, respectively), and Air Cal (bought by American for $225 million), *combined*.[50] For these investments, those airlines acquired significant operating assets and market share. As a result of the LBO, Northwest acquired nothing more than burdensome debt.

The need to pay down debt may well have motivated Northwest to protect its monopoly hub status against incursions by low-cost/low-fare competitors. Only in the absence of competition could Northwest hope to maintain prices at supracompetitive levels.

B. Northwest Struggles With the Debt Burden

By the early 1990s, Price Waterhouse concluded that Northwest was at a "critical juncture" and was facing "significant hurdles."[51] Most stemmed from the $3.65 billion leveraged buy-out of the company by Alfred Checchi and partners (Wings Holdings, Inc.) in 1989, which saddled an almost debt-free company with enormous debt.[52] Both mergers and route sales were explored to shore up its financial condition and strategic

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49. In the matter of the Acquisition of Northwest Airlines by Wings Holdings, Inc., DOT Order 91-1-41 (1991), at 2.

50. Dempsey, *supra* note 31 at 127-29.

51. *See* Asra Q. Nomani, *Global Dogfight: World's Major Airlines Scramble to Get Ready for Competitive Battle*, WALL ST. J., Jan. 14, 1992, at A8.

52. *See* Asra Nomani, *NWA Weighs Sale of Routes, Merger Option*, WALL ST. J., Feb. 11, 1991, at A3.

position.[53] In 1990, Northwest's pension was underfunded by $78 million.[54]

According to one source, the heavy debt burden put on by the Checchi LBO, coupled with these tremendous losses, caused Northwest's debt-to-equity ratio to soar to an unbelievable 30 to 1 ($4.2 billion in debt versus $141 million in equity).[55] The LBO so loaded Northwest with debt that, in order to avoid Chapter 11, Northwest deferred aircraft deliveries, persuaded banks to defer loan payments, convinced labor to take deep wage cuts in exchange for stock, and persuaded the State of Minnesota to engage in the largest public bail-out in the history of commercial aviation.

C. Northwest's Fleet Age Ascends

The massive debt burden imposed by the LBO also made it difficult for Northwest to retire aging aircraft. Northwest opted instead to hushkit and refurbish all of its DC-9s whose average age was then 24 years, so as to be able to fly them another 15 years.[56] The cost of a hush-kit is about $1.5 million per aircraft, or as much as $18 million if new avionics, engines, and cabin interiors are added. This compares favorably with the $30-$35 million cost of a new aircraft.[57]

As a result of hush-kitting and new aircraft cancellations, by the dawn of the 21st Century, Northwest Airlines had the oldest fleet of aircraft of any major airline by a significant margin, surpassing even TWA's fleet for that ignoble distinction.[58] In 1991, Northwest's fleet was 35% older than the industry's average; by 1998, Northwest's fleet was 60% older than the industry's average. According to the 2001 Global Fleet Handbook, Northwest continues to have the oldest fleet at 20.4 years.[59]

D. Labor Bails Out Northwest

After the Checchi LBO, annual interest expenses at Northwest rose to $7,835 per employee, compared to $2,534, $1,612 and $928 at United,

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53. *See id.*

54. *Three Majors Among Top 50 Firms With Underfunded Pensions*, Aviation Daily, Nov. 26, 1991, at 355.

55. Jonathan Laing, *Losing Altitude: Heavy Debt Load, a Legacy of Its LBO, Weighs Down NWA*, Barron's, Feb. 17, 1992, at 8. Others estimated that Northwest carried $1.4 billion in debt. Lollar, *It's Not Easy Being Fourth . . . Or Fifth*, Frequent Flyer, Nov. 1991, at 8, 12.

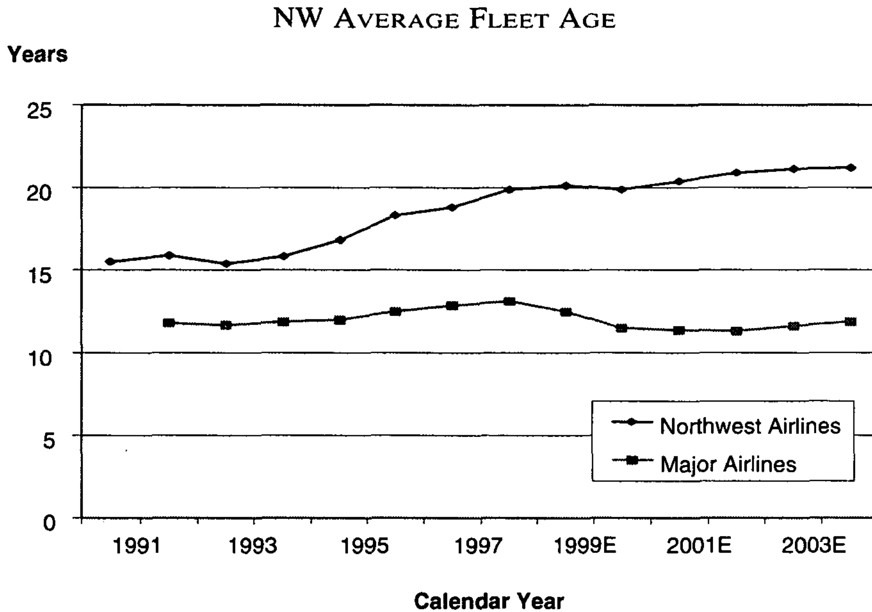
56. Susan Carey, *Northwest Airlines Plans to Renovate Some DC-9s Rather Than Replace Them*, Wall St. J., Aug. 9, 1994, at A2.

57. Jeff Cole, *McDonnell Embarks On a New Course for Old Planes*, Wall St. J., July 26, 1993, at 16A.

58. Data for the chart are drawn from CIBC World Markets, Aircraft Fleet Analysis (Oct. 5, 1999).

59. *Fleet Study Sees Overcapacity, Aging Planes at Northwest*, Aviation Daily, March 27, 2001 at 3.

NW AVERAGE FLEET AGE



Source: Salomon Smith Barney

American and Delta, respectively.[60] In 1993, labor surrendered $886 million in concessions over three years, in exchange for 33% of the company's stock. By 1994, despite several profitable quarters, Northwest was still struggling to refinance $4 billion in debt, with a $1.7 billion note due in 1997.[61] A balloon payment of $731 million due in the year 2000 was rescheduled to be paid out over three years beginning in 2005; that debt was taken off the books as long-term debt and treated as a minority interest in an affiliated company.[62] Yet belt-tightening would not reach senior management. In 1995, Northwest's John Dasburg pocketed a salary and bonus of more than $800,000, and $8.7 million in stock options.[63] In 1998, Dasburg reaped $16.7 million by exercising stock options. He reported compensation of $3.65 million in 1999.[64]

E. THE STATE OF MINNESOTA BAILS OUT NORTHWEST

Northwest also turned to the State of Minnesota to help it out of the

60. Laing, *supra* note 55 at 8.

61. Steven Lipin & Carl Quintanilla, *NWA May Turn to Modest Loan Plan, As Larger Credit Is Said to Worry Banks*, WALL ST. J., Oct. 17, 1994, at A4.

62. *Northwest Restructures $731 Million In Debt*, AVIATION DAILY, Oct. 27, 1995, at 155.

63. Susan Carey, *Northwest Air's Chief Got $8.7 Million From Exercising Stock Options in 1995*, WALL ST. J., Apr. 8, 1996, at 4A.

64. Tony Kennedy, *Union Leader Assails NWA Executive In Letter*, MINNEAPOLIS STAR-TRIBUNE, Apr. 14, 2000, at D1.

financial morass created by the LBO. It successfully lobbied the State legislature to sell $250 million in bonds on behalf of Northwest Airlines to finance construction of a maintenance facility in Duluth, and $100 million for a engine repair facility in Hibbing.[65] In 1991, the State of Minnesota gave an incentive package worth $838 million to Northwest Airlines to build an aircraft maintenance complex in the state.[66] Included was $320 million in low-interest loans provided by the Metropolitan Airports Commission, operator of the Minneapolis/St. Paul Airport, as well as $350 million in bonds to construct the complex.[67]

Ultimately, $47.7 million in revenue bonds were issued by the State of Minnesota to finance the design, construction and equipping of Northwest's Airbus heavy maintenance facility. Collateral for the loan consists of the facility, and Northwest's Detroit-Paris route. The Metropolitan Airports Commission issued $270 million in general obligation revenue bonds, for which it acquired Northwest's flight training center at Eagan, certain other property at the airport, and refinanced certain leasehold interests of Northwest. Collateral for the bonds exists in the form of airport facilities, airport building components, aircraft engine parts, and certain international routes. An additional $9.7 million was issued to Northwest in the form of forgivable loans to build and equip a reservations system at Chisholm.[68]

Minnesota taxpayers now were not only paying among the highest air travel fares in the nation, their state government was providing subsidies to an airline which had created a monopoly at the airport their federal taxes had built. Ironically, Northwest spokesman Jon Austin would later complain that Sun Country and other new entrant airlines were trying to win "at the government dole" what they could not win in the free market.[69]

V. Northwest Accuses American Airlines of Predatory Pricing

A. Value Pricing

In April 1992, American Airlines introduced "Value Pricing", an attempt to simplify the increasingly chaotic airline fare structure which had

65. Debra Werner, *Northwest Airlines, Minnesota Put Maintenance Hubs Back on Agenda*, COM AVIATION NEWS, Aug. 23, 1993, at 10.

66. *Minnesota Legislature Gives Final Approval to Northwest Incentive Package*, AVIATION DAILY, Dec. 17, 1991, at 474.

67. *See id.*

68. Minn. Dep't of Fin., Presentation to the Legislative Commission on Planning and Fiscal Policy (2000).

69. Tony Kennedy, *Sun Country: NWA Abuses Low Milwaukee Fares*, MINNEAPOLIS STAR TRIBUNE, July 26, 2000, at D1.

evolved under deregulation. Though American Airlines had introduced yield management in the 1980s as a strategic tool to maximize revenue relative to the demand characteristics of different classes of travelers, by the 1990s, American concluded that the Byzantine pricing structure was unduly complex, and that the highest fares were dissuading business travelers from taking trips. Value Pricing reduced American's fares to a simplified four-tiered pricing approach – first class, regular coach, a 14-day advance purchase, and a 21-day advance purchase. American believed that the existing pricing structure created too large a gap between the highest and lowest fares, introducing Value Pricing in order both to simplify the fare structure, and to lower the highest prices and raise the lowest ones.[70] The unrestricted coach fares, then used by only 6% of travelers, were reduced between 38%-40%.[71] Though American anticipated the new fare structure initially would cost it money, American believed Value Pricing would be profitable after an inaugural period, and that consumers would appreciate and benefit from a simplified pricing structure.[72]

B. Grownups Fly Free

The leadership American attempted to exert to simplify the fare structure evaporated when, on May 26, 1992, Northwest Airlines responded with its "Grown-Ups Fly Free" promotional fare, whereby an adult would receive a free ticket if accompanied by a fare-paying child. In order to preserve the integrity of its four-tier Value Pricing structure, on May 27th American met Northwest's pricing initiative by slashing its lowest advance-purchase fares in half.[73] The result was a financially troubling period for the industry as prices spiraled downward.[74] Ultimately, fare proliferation re-emerged, with all of the complexity and volatility of before. The price wars were highly destructive to airline balance sheets. Coupled with recession and high fuel prices, the airline industry suffered the worst losses in its history during this period.

C. Northwest's Predatory Pricing Lawsuit Against American Airlines

After several months of sustaining enormous losses, Northwest and

70. *Crandall Calls Fare Cuts Fair*, Associated Press, July 29, 1993.

71. Lawrence Kaufman, *Discipline, Deregulation Don't Really Go Together*, Journal of Commerce, Aug. 30, 1993, at 11.

72. Kathryn Jones, *Airlines' Shootout In Texas Court Proves a Dud*, N. Y. Times, July 29, 1993, at D1.

73. Richard M. Weintraub, *Rivals Challenge American Airlines in a Texas Court*, Wash. Post, July 10, 1993, at F1.

74. Joan M. Feldman, *The Price of Retribution*, Air Transport World, Dec. 1992, at 54.

Continental filed a lawsuit contending that American Airlines had dropped fares in an effort to drive them out of business. They alleged that American Airlines introduced the simplified Value Pricing plan as a means of implementing its long-term strategy of persuading its competitors to charge higher prices, limiting price competition, and disciplining competitors which failed to follow American's price signals, as well as driving most other carriers from the market.[75] Northwest alleged that American Airlines' "predatory and exclusionary conduct . . . was undertaken for the specific purpose . . . of accomplishing precisely what [American Airlines CEO Bob] Crandall has sought – the elimination of competitors . . . and the financial weakening of . . . Northwest." Northwest further contended that American was "offering discounts for a far greater number of passengers and incurring substantial revenue losses to itself, which were avoidable if it had merely matched Northwest's limited promotional fares." According to Northwest, smaller rivals were forced to charge the fare structure dictated by American, or "suffer imposition of progressively lower and unremunerative pricing levels that would lead them even more quickly to extinction."[76] Northwest alleged that American engaged in "illegal, anticompetitive and monopolistic activities" which were "intended to further its goal of eliminating competition."[77]

Contending that American Airlines was a ruthless schemer trying to ground Northwest with below-cost pricing, Northwest Chairman Gary Wilson said, "American almost drove us out of business."[78] The losses, after special charges, of nearly more than $1 billion in 1992, caused Northwest to seek concessions from lenders and its 40,000 employees.[79] No mention was made of the $3 billion leveraged buy-out of Northwest as a cause of Northwest's ill health. Referring to American's CEO Bob Crandall, Wilson said "It's not fair. . . . It's time the bully in the schoolyard got punched."[80] Wilson claimed that American's fare cuts were designed to bleed rivals into their graves. "Natural death is not a

75. *Continental Airlines, Inc. v. American Airlines, Inc.*, 824 F. Supp. 689, 692-93 (S. D. Tex. 1993).

76. Josephine Marcotty & David Phelps, *NWA Suit Says American Is Trying to Drive Competitors Out of Business*, MINNEAPOLIS STAR TRIBUNE, June 13, 1992, at 1A.

77. Isae Wada, *Northwest Joins Legal Attack on AAL's Pricing Practices*, TRAVEL WEEKLY, June 18, 1992, at 4.

78. Terry Maxon, *Northwest Execs Say AA Almost Ruined Airline,* DALLAS MORNING NEWS, July 15, 1993, at 1D.

79. *Northwest Airlines Reports Losses Widen*, UNITED PRESS INT'L, Feb. 4, 1993.

80. Stephen D. Solomon, *The Bully of the Skies Cries Uncle*, N.Y TIMES MAGAZINE, Sept. 5, 1993, at 6-13. Crandall would deride Northwest's managerial ineptitude in acquiring the airline in a highly leveraged buy-out, then failing to run it profitability, saying, "Northwest's management is Northwest's problem." Josephine Marcotty & David Phelps, *NWA Suit Says American Is Trying to Drive Competitors Out of Business*, MINNEAPOLIS STAR TRIBUNE, July 13, 1992, at 1A.

problem," said Wilson. "It's murder where there's a problem."[81] Wilson would also deride the low-fare carriers, describing Southwest Airlines as "clearly a 'cancer' that is going to plague the airline industry . . . ."[82]

Northwest CEO John Dasburg claimed that American's response to Northwest's "Grown-Ups Fly Free" promotion was not legitimate price competition, "It is predatory pricing, deliberate pricing below profitable levels to undercut competition to the point that few airlines will survive." Dasburg insisted, "In the long run, predatory pricing will reduce the number of airlines, ultimately cutting the number of flights and choices available, particularly in smaller markets. This will leave the few surviving airlines free to price just as high as they want for just as long as they want. You will bear the cost of this."[83]

Northwest Airlines' top government affairs official, Elliot Seiden, echoed these sentiments, saying, "I cannot recall any airline ever suing any other airline for predatory pricing, no matter how rough things have gotten. I can't recall any airline so blatantly and openly trying to destroy the business of other companies."[84] Nonetheless, the jury was unpersuaded, promptly issuing a verdict for American Airlines.

Ironically, the allegations that Northwest levied against American are virtually the same allegations low-fare carriers such as Reno, Spirit, Pro Air, Western Pacific, Kiwi, Access Air, ValuJet/AirTran, Vanguard, and Sun Country Airlines have levied at Northwest. Whether or not American's pricing practices against Northwest were predatory, it was clear at the time that Northwest's executives were clearly sympathetic to the plight of a smaller carrier in a larger carrier's cross-hairs.

After losing its predatory pricing lawsuit, Northwest transformed itself from prey into predator.

VI. Northwest's Response to New Entrant Airlines

An established carrier which finds its spokes assaulted by a new entrant typically will cut prices and, sometimes, expand capacity, to discipline the competitor. Both will lose money, but large carriers have the ability to cover short-term revenue losses from profits derived from less competitive markets, and have stronger balance sheets with which to weather the financial storm.[85] Before becoming Executive Vice President

81. Mike Myers, *NWA Calls Rival's Chiefs Ruthless Schemers*, Minneapolis Star Tribune, July 15, 1993, at 1A.

82. Terry Maxon, *Northwest Execs Say AA Almost Ruined Airline*, Dallas Morning News, July 15, 1993, at 1D.

83. David Phelps, *NWA Asks Pilots for Giveback of $500 Million*, Minneapolis Star Tribune, July 14, 1992, at 1A.

84. Kirk Victor, *Sky Kings*, The Natl. Journal, July 25, 1992, at 1722.

85. Peter C. Carstensen, *Evaluating 'Deregulation' of Commercial Air Travel: False Dichot-*

at Northwest Airlines, Michael Levine pointed out that, typically, the major airlines offer the low fare only on local origin-and-destination [O&D] traffic on flights in close time proximity to the new entrant's, extracting higher yields from passengers arriving and departing from monopoly spokes. According to Levine, this revenue advantage may neutralize the new entrant's cost advantage and will deleteriously impact its staying power.[86] Levine noted, "The ability of an incumbent to respond rapidly and cheaply to the prices and output of new entrants contradicts perhaps the most critical assumption of contestability theory."[87] Levine set out a blueprint by which an incumbent airline can destroy a new entrant:

> The essence of the strategy is simple. Match, or better yet beat, the new entrant's lowest fare with a low fare restricted to confine its attractiveness to the leisure-oriented, price-sensitive sector of the market. Match business-oriented fares and offer extra benefits to retain the loyalties of travel agents and frequent fliers. Add frequency where possible, to "sandwich" the new entrant's departures between one's own departures. Make sure enough seats are available on your flights in the market to accommodate increases in traffic caused by the fare war. In short, leave no traveler with either a price or schedule incentive to fly the new entrant. If the new entrant attempts to lower prices . . . , the incumbent matches, no matter how low the fare. The object is to reduce trial and to subject the new entrant to a prolonged period of operation at low load factors. This strategy saps the entrant's working capital while inhibiting trials that would disseminate favorable information about the new entrant.[88]

Northwest argues that it is only *matching* its rivals' fares, not undercutting them. Yet, why would Northwest add seat and flight frequency capacity to markets in which its revenue per seat was declining, if not for the impact it has on forcing the new entrant to suffer declining load factors and yields, and ultimately to withdraw? As the Department of Transportation has observed:

> A low-fare airline's entry should not usually require the incumbent airline to match the new entrant's fare levels and make a large number of seats available at those levels or to eliminate restrictions on its discount fares. Network airlines, after all, typically offer service features unmatched by most low-fare airlines. Professors Oster and Strong correctly point out that airlines compete on many service features, not just price. The network airlines themselves justify hub fare premiums by contending that the superior service offered by the hubbing airline makes business travelers and others willing to

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omization, Untenable Theories, and Unimplemented Premises, 46 WASH. & LEE L. Rev. 109, 126 (1989); Russell A. Klingaman, *Predatory Pricing and Other Exclusionary Conduct in the Airline Industry*, 4 DEPAUL BUS. L.J. 281 (1992).

86. Michael E. Levine, *Airline Competition in Deregulated Markets: Theory, Firm Strategy, and Public Policy*, 4 YALE J. ON REG. 393, 451 (1987).

87. *Id.* at 452.

88. *Id.* at 393.

pay the higher fares. As the state attorneys general point out, 'Concern of the fate of the public's access to low fares rings hollow in light of the fact that all airlines are entirely free to offer low fares right now on any route they serve and to commence low fare service today whenever they like.' Network carriers have failed to show that increasing capacity and the availability of discount seats to meet the demand for low-fare travel and eliminating restrictions on discount fares become rational goals after entry by a low fare airline, but not before entry.[89]

The weapons with which an incumbent megacarrier attacks a new entrant in the city-pairs in which it inaugurates service include the following:

- Dropping prices sharply;
- Eliminating advance purchase and Saturday night stay-over restrictions;
- Expanding the inventory of low-fare seats offered;
- Increasing the number of flights and/or the size of aircraft;
- Scheduling departures in close proximity to the new entrant's flights, sometimes boxing them in;
- Offering passengers bonus frequent flyer miles;
- Paying travel agent commission overrides to steer traffic toward the incumbent in the new entrant's markets;
- Paying higher upfront commission rates on routes where it competes with a new entrant;
- Biasing its computer reservations systems against non-affiliated interline connections;
- Refusing to enter into ticketing-and-baggage, joint-fare, and code-sharing relationships with the new entrant;
- Refusing to lease gates, provide services, or sell parts to the new entrant;
- Restricting airport operators with majority-in-interest clauses to prohibit the construction of gates and other infrastructure for new entrants; and
- Prohibiting affiliated regional feeder airlines from entering into marketing agreements with the new entrant.

At the same time, the incumbent airline maintains its monopoly fares and low service levels in markets where it faces no competition (or competes only with another megacarrier in a tacit "live-and-let-live" environment), allowing the incumbent to earn supracompetitive profits with which to cross-subsidize the losses it incurs as it attempts to bleed the new entrant into eventual submission and withdrawal. After the new entrant withdraws, the incumbent airline typically raises prices sharply.

89. U.S. Dep't of Transp., *supra* note 10.

A. Northwest vs. Reno Air

Reno Air began operations out of Reno, Nevada, in July 1992. On February 10, 1993, Reno Air, then flying only seven jets, had the temerity to announce its intention to inaugurate thrice daily round-trip service between Reno and Minneapolis on April 1 at a fare of $95 one-way. Northwest had abandoned the route in 1991, because it was unprofitable. The day after Reno Air announced it would inaugurate Reno-Minneapolis service, Northwest retaliated by announcing it was beginning three round-trip daily flights between Minneapolis and Reno on April 1.[90] The following day, Northwest announced it would begin new service to Reno, Nevada, from three of the West Coast cities served by Reno Air – Seattle, Los Angeles, and San Diego – on April 1, in effect, establishing a Northwest mini-hub at Reno, Nevada. These were routes not theretofore flown by Northwest. On May 1, 1993, Northwest announced it would begin a second daily flight to both Los Angles and Seattle to Reno. Northwest began offering bonus frequent flyer miles to passengers flying it from Reno, Nevada, and commission overrides to travel agents booking passengers on Northwest.[91] Northwest also announced that it would match Reno Air's fares, as low as $55 one-way over some segments.[92] Northwest offered the same fares on its *nonstop* flights from Minneapolis to Los Angeles, San Francisco, San Diego, Seattle, Ontario, and Portland as Reno Air offered to these cities in *connecting* service. By May 20th, the losses sustained caused Reno Air to reduce Minneapolis service to one flight per day.[93]

Sen. Richard Bryan (D-Nev.) asked the Departments of Justice and Transportation to investigate whether Northwest was using "predatory pricing and scheduling practices" to run Reno Air out of business. According to Sen. Bryan, "The federal government should not let Northwest snuff out this airline just as it is getting its wings."[94] DOT Secretary Federico Pena met with Northwest Airlines officials in March 1993, and gave them just two days to reconsider, or face the wrath of DOT. Northwest responded by abandoning its plans to start service to Reno from Seattle, Los Angeles, and San Diego, but continued its Minneapolis-Reno

90. Alexandra Marks, *Frequent Fliers Sue Over High Fares at Hubs*, Christian Science Monitor, August 29, 2001, at 2.

91. Oster, *supra* note 2 at 25. The authors point out that commission overrides also played a role in the decision of Southwest Airlines to exit the Indianapolis-Detroit market, one of the few it has ever withdrawn from, and of Midwest Express to abandon the Milwaukee-Detroit market.

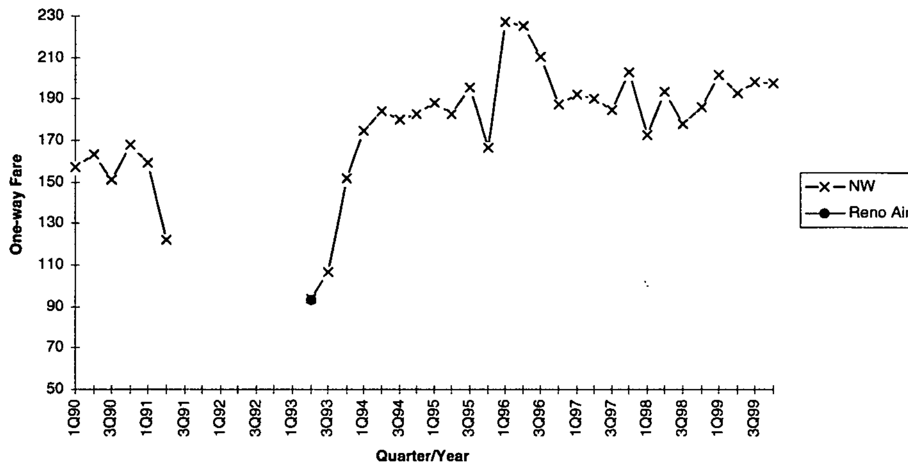
92. Frank Costello, *Is That a Predator Up There?*, Journal of Commerce, May 11, 1993, at 8A.

93. Oster, *supra* note 2.

94. Earle Eldridge, *Bryan Calls for Probe of Reno Air's Competitors*, Joyce Communications, Mar. 3, 1993.

service.[95] Northwest retreated after DOT Secretary Federico Pena tacitly threatened regulatory or antitrust action.[96] But Reno Air was forced to abandon the Minneapolis-Reno market, ceasing service on June 1, 1993.[97] According to Professors Oster and Strong, "Following Reno's exit from the Reno to Minneapolis market, [Northwest's] fares increased quickly and steadily.[98] After Reno Air's withdrawal, Northwest's lowest fare increased 73% from $86 to $149, while its lowest refundable fare increased 320%, from $136 to $455. By the Spring of 2000, Northwest's lowest seven-day advance purchase fare was $1026.[99]

MINNEAPOLIS-RENO AVERAGE FARE



Source: US Department of Transportation; Passenger Origin-Destination Survey.

Decrying Northwest's "blatantly anticompetitive responses", Reno Air's General Counsel Bob Rowen alleged, "Northwest entered with excess capacity and reduced its fares. Industry experts agree that Northwest's purpose in doing so was to destroy the market, to push Reno Air out and deter other low fare airlines from entering Northwest's hubs."[100]

95. *Northwest Forced to Drop Its Reno Plans*, FLIGHT INTL, Apr. 7, 1993.

96. Mark T. Clouatre, *The Legacy of Continental Airlines v. American Airlines: A Re-Evaluation of the Predatory Pricing Theory in the Airline Industry*, 60 J. AIR L. & COM. 869, 914 (1995).

97. Oster, *supra* note 2.

98. *Id.*

99. *Competition in the Airline Industry Before the Antitrust, Business Rights, and Competition Subcomm. of the S. Judiciary Comm.* (May 2, 2000) (testimony of Bill LaMacchia, President and CEO, Sun Country Airlines).

100. *Predatory Pricing in the Airline Industry Before the S. Comm. On Com., Sci. and Transp.* (Oct. 28, 1997) (testimony of Bob Rowen, Vice President and General Counsel, Reno Air Inc.).

In 1997, Reno Air filed an antitrust lawsuit against Northwest alleging unlawful monopolization. The suit contended that Northwest employed similar anticompetitive conduct against People Express, Icelandair, Midway Airlines and other new entrants at Minneapolis/St. Paul.[101] According to Rowen, Northwest "engaged in a variety of tactics, including below-cost pricing, to drive us from the market. These actions were predatory."[102] The case was dropped in April 1999, after American Airlines purchased Reno Air.[103]

B. Northwest vs. Spirit Airlines

In 1996, the U.S. Department of Transportation found that Detroit was one of the four most expensive airports in the nation. It also found that Northwest, which carried 74% of Detroit's passengers, was the nation's most expensive airline, particularly on flights of less than 750 miles, where it has little competition.[104]

The high fares attracted new entrants. Formerly a Detroit charter carrier, Spirit Airlines began offering once-a-day scheduled flights between Detroit and Philadelphia, on December 15, 1995. Northwest's domination of Wayne County/Detroit International Airport prohibited Spirit from leasing gates, except on an *ad hoc* basis. Spirit's introductory round trip fares in the market were between $49 and $139. In the first quarter of 1996, Spirit carried fewer than 12,000 passengers at fares between $50 and $75, while Northwest carried only about 1,200 passengers at those fares. In the second quarter of 1996, Spirit introduced a second round-trip, which increased its traffic 57%, to nearly 19,000 passengers; Northwest's traffic increased 36%, though its traffic in the $50-75 range increased only 11% to 1,360. During that quarter, Spirit also entered the Detroit-Boston market.[105]

But in the third quarter of 1996, Northwest unloaded 35 times the number of low-fare seats in the Detroit-Philadelphia market as it had offered previously, causing a 37% decline in Northwest's revenue.[106] Professors Oster and Strong point to this example as illustrating the ability of incumbent airline to open the inventory of seats for sale at low fares to consume low-fare demand, saying, "The airline could, for example, offer service at low average fares by simply making a large number of seats

101. Tony Kennedy, *Reno Air Files Suit Against NWA*, Minneapolis Star Tribune, Apr. 17, 1997, at 1D.

102. George Raine, *Battle On High*, S.F. Examiner, May 22, 1998, at C-1.

103. Katherine Yung, *Fair Fairs*, Dallas Morning News, Mar. 1, 2000, at 1D.

104. Mike Brennan, Dan Fricker & Gerry Volgenau, *U.S. Is Looking at Fares at NWA*, Detroit Free Press, Feb. 28, 1998, at 9B.

105. Oster, *supra* note 2.

106. *Id.*

available in the lower fare categories, as Northwest did in the third quarter of 1996 in the Detroit to Philadelphia market."[107] Northwest's previous lowest fare was $100 higher and had required a 21-day advance purchase and Saturday night stay. Northwest matched Spirit's fares, not only on competitive time slots, but on all of Northwest's 11 daily flights to Boston, and its seven flights to Philadelphia.[108] Spirit's load factor in the market fell from 86% in the second quarter, to 39% in the third quarter. Spirit was forced to withdraw from the Detroit-Philadelphia market on September 30, 1996. After Spirit's withdrawal, Northwest reduced the number of low-fare seats in the market to 27,100 in the fourth quarter, and flew only 910 seats at that level in the first quarter of 1997.[109]

Testifying before a U.S. Senate Transportation Subcommittee, Mark Kahan, Vice Chairman of Spirit Airlines, said,

> "In June 1996, we began hearing rumors that 'Northwest will unload on Spirit' in the Detroit-Philadelphia market. And that is what happened. On June 30, 1996, Northwest 'matched' Spirit's $49 fare in the Detroit-Philadelphia market on all flights and simultaneously increased its capacity by more than 15 percent over the previous year." [110]

Kahan testified that after Spirit entered the Detroit-Philadelphia market, Northwest dropped its yields 54% while increasing its capacity 15%. Sharply reduced prices coupled with capacity dumping allegedly forced Spirit to withdraw from the Detroit-Boston and Detroit-Orlando markets as well. Said Kahan:

> "It is probable that Northwest sacrificed out-of-pocket losses not less than $10 million because of its fare decreases and capacity increases in the Detroit-Boston and Detroit-Philadelphia markets in the third quarter of 1996 alone. These actions clearly made no *sense* unless Northwest was confident that Spirit would be obliged to exit the market. . . . You will pardon us for believing that Northwest tried to put Spirit out of business in the third quarter of 1996." [111]

Spirit was forced to withdraw from the Detroit-Boston market on September 8, 1996, and from the Detroit-Philadelphia route on September 30, 1996. Within several months, Northwest's fares climbed dramatically. By early 1998, Northwest's lowest fare was $275.[112] According to Northwest spokesman, Jim Faulkner, "We don't feel like we've done any-

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107. *Id.*

108. Brennan, *supra* note 104.

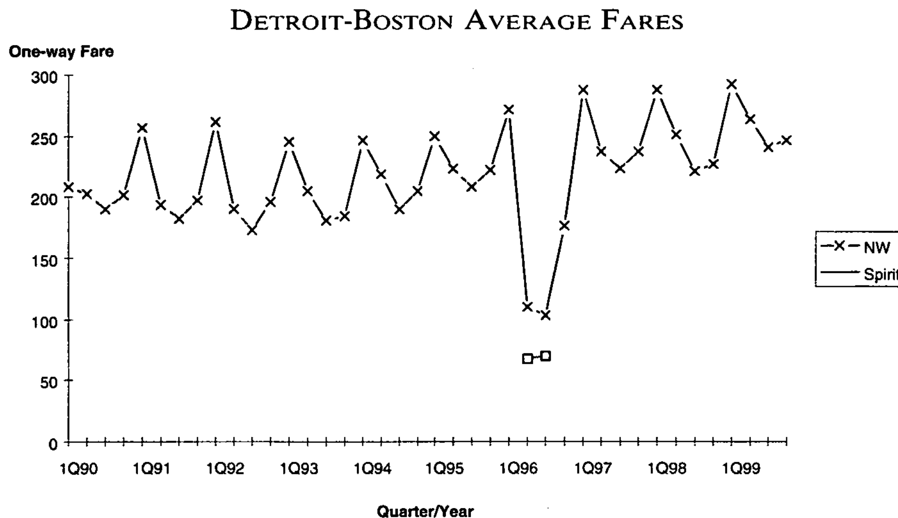
109. Oster, *supra* note 2.

110. Marsha Stopa, *Predatory Pricing?: Small Airlines Are Taking On the Majors*, CRAIN'S DETROIT BUS., Mar. 16, 1998, at 1.

111. *House Comm. on Transp. and Infrastructure Aviation Subcomm. (Apr. 23, 1998) (testimony of Mark S. Kahan, Vice Chairman and Chief Operating Officer, Spirit Airlines).*

112. Brennan, *supra* note 104.

DETROIT-BOSTON AVERAGE FARES



Source: US Department of Transportation; Passenger Origin-Destination Survey.

thing wrong."[113]

In March, 2000, Spirit filed an antitrust suit against Northwest, alleging that Northwest engaged in unlawful monopolization. Spirit contended that Northwest's domination of Detroit "is the intended consequence of a cleverly crafted avaricious scheme by Northwest to exclude competition in order to raise ticket prices at Detroit to unjustifiable levels that thoroughly demonstrate the absence of a competitive market."[114] Spirit further alleged that Northwest cut its fares to below-cost levels and flooded the routes with additional capacity after Spirit introduced discount fares in what had theretofore been Northwest's monopoly nonstop routes.[115]

C. Northwest vs. Pro Air

Pro Air inaugurated service from Detroit City Airport to Baltimore on July 4, 1997, offering fares 60% lower than Northwest's at Detroit Metro Airport. Within a month, it had begun service to Indianapolis, Newark, and Milwaukee.[116] In a fax to travel agents, Northwest announced it was offering a 20% commission – then twice what was custom-

113. Stopa, *supra* note 110.

114. Ricardo Thomas, *Unfriendly Skies: Market Domination*, DETROIT NEWS, July 20, 2000, at A-1.

115. John Gallagher, *Sprit Sues Northwest in Detroit*, DETROIT FREE PRESS, Mar. 30, 2000, at 1C.

116. Carole A. Shifrin, *Detroit City Startup Sets Low-Fare Strategy*, AVIATION WEEK & SPACE TECH, July 28, 1997, at 46.

ary – on tickets sold in markets Pro Air had entered.[117] Northwest matched Pro Air's $59 one way fare in the Detroit-Milwaukee market until Pro Air withdrew on February 5, 1998. According to Pro Air's COO Craig Belmundo, Northwest raised its fares to $130 on the afternoon of Pro Air's withdrawal, an allegation Northwest denied.[118] Pro Air CEO Kevin Stamper said, "They match us on our prices on every flight, and every seat."[119]

Before Pro Air inaugurated flights from Detroit City Airport to Baltimore, Indianapolis, Milwaukee and Detroit, Northwest offered one-way fares to these cities of between $180 and $221. After Pro Air entered these markets, Northwest matched ProAir's fares of $59 to $79. In addition to withdrawing from Milwaukee, ProAir was forced to reduce service to Indianapolis from two flights per day, to one. Northwest's Richard Hirst observed that its Detroit and Minneapolis hubs "are highly competitive. . . . Congress never expected there to be perfect competition in air services." ProAir's Chairman Kevin Stemper replied, "predatory activities on the part of carriers that already possess many competitive advantages may drive small airlines out of the industry and lead to monopolies and market abuse."[120]

D. Northwest vs. Western Pacific Airlines

Founded by Ed Beauvais (who earlier had founded America West Airlines), Western Pacific Airlines inaugurated service from a base at Colorado Springs, Colorado, in 1995. By 1996, Western Pacific was serving 16 cities from Colorado Springs with 15 Boeing 737-300 aircraft.

Before Western Pacific started up operations at Colorado Springs, Northwest had not served the city. Northwest's ordinary pattern of adding a new city to its network was not to add service from each of its three domestic hubs simultaneously—it was instead to begin by serving the new city from Detroit, and if that was financially successful, expanding service from Minneapolis, and perhaps eventually Memphis. But in 1996, after Western Pacific began to grow, and after Northwest learned that Western Pacific was seeking gates at Detroit, Northwest quickly inaugurated service to Colorado Springs from each of its three hubs – Minneapolis, Detroit and Memphis. The message was clear—Western Pacific would be unwelcome at Northwest's hubs, would be met with fierce opposition, lots of seats and low fares. By the Fall of 1997, Western Pacific had withdrawn from its Colorado Springs hub, and was liquidated the

117. Brennan, *supra* not104.

118. Stopa, supra note 110.

119. Steve Lott, *Pro Air Stalled By Software Problems*, Aviation Daily, Nov. 15, 1999, at 3.

120. Kenneth Cole, *Northwest Accused of 'Predatory Tactics'*, Detroit News, Apr. 2, 1998, at B3.

following year. With Western Pacific's exit, suddenly Northwest's interest in Colorado Springs disintegrated, and it terminated service there from its Detroit and Memphis hubs.

E. Northwest vs. Kiwi International

Newark-based upstart airline Kiwi International Airlines accused Northwest of predatory practices in the Fall of 1998. Kiwi contended it was forced to pull out of the Minneapolis-Detroit and Minneapolis-Newark markets after Northwest and Continental Airlines matched Kiwi's prices on all their flights.[121] They began by matching Kiwi's $79 fare. Once Kiwi dropped the fare to $69, they matched that too. Kiwi's full flights were soon half empty. Once Kiwi exited the market, Northwest raised fares in the Minneapolis-Detroit market to $467.[122]

F. Northwest vs. Access Air

Des Moines-based Access Air accused Northwest of predatory practices in 1999.[123] Even though Access Air did not fly to Minneapolis,[124] Northwest and two other carriers matched and lowered Access Air's introductory fares of $198 round trip for flights between Los Angeles and New York, and between Los Angeles and Des Moines, or Moline, Ill. .[125] Access Air then attempted to raise its fares to $298 round trip – substantially less than the $380 to $480 the carriers previously charged for a 14-21 day advance purchase, and the $680 they had charged for a 7-day advance purchase. The majors refused to match the increase and continued to offer the $198 round trip fare.[126] Access Air accused the carriers of below-cost pricing in order to drive it out of business. "Unfortunately, the expected bear hug by the major airlines has begun," said Access Air President Robert Ferguson. "Three of the [major airlines] are now offering fares in Access Air markets that are one-third below our fares – and far below both their normal fares and their costs. If continued, these fares will force us out of business."[127]

Neither Kiwi International nor Access Air nor Pro Air nor Western Pacific is still flying. As Ed Faberman, director of the Air Carriers Asso-

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121. Minnesota Planning, supra note 15.

122. John Schmeltzer, *Kiwi Says Giants Priced It Out of a Market*, Chi trib., Oct. 2, 1998, at 2.

123. Katherine Yung, *supra* note 103.

124. Northwest Rebuttal, *supra* note 5.

125. Chris Olson, *Regional Fare Game Eppley flights, Fees Draw Passengers from All Over*, Omaha World-Herald, Mar. 27, 1999, at 47.

126. Frank Swoboda, *New Airline Accuses Rivals of Predatory Pricing Tactics*, Wash. Post, Mar. 17, 1999, at E-3.

127. Swoboda, *supra* note 126.

ciation of America, observed when financially injured by the predatory behavior of a major airline, "Most new carriers could not survive the time and money it takes to file [an antitrust] lawsuit."[128]

G. Northwest vs. ValuJet/AirTran

Northwest responded to ValuJet's entry into the Atlanta-Memphis market by dropping its average fares 54%, from $122, in the quarter immediately preceding ValuJet's entry, to $56 in the quarter following its entry. From the fourth quarter of 1994 until the first quarter of 1997, Northwest's average fares were consistently lower than ValuJet's. Since January 1994, Northwest has offered an average fare of $55.93, lower than ValuJet's average fare of $56.13. Since Northwest offers a 1st Class product (which during most of the quarters for which data is available, ValuJet—now AirTran—did not), and since the DOT data includes first class in the average fare base, Northwest is underpricing AirTran in its coach product by a significant margin.[129]

According to AirTran, not only had Northwest cut its yield to less than half its level six months prior to Valujet's entry into the market, Northwest also increased its capacity by more than 50% in the Atlanta-Memphis market beginning in late 1994.[130]

Why does Northwest charge 37% more than Southwest in the St. Louis-Detroit market, and less than ValuJet in the Atlanta-Memphis market? The likely answer is predatory intent, which emerges depending on the perception of economic strength of the target. Northwest realizes it cannot drive Southwest from the market, but that ValuJet/AirTran might be driven from it.

AirTran also complained to the DOT that Northwest boosted seat capacity in the Minneapolis-Atlanta market after AirTran announced it would begin service there in June 2000.[131] AirTran says Northwest switched to larger planes on the Atlanta-Minneapolis route, increasing its average daily seat count by about 40 percent. "That kind of increase goes well beyond reasonable competition," AirTran marketing director Tad Hutcheson said. "It's almost as many seats as we were going to put in the market."[132]

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128. Kristin S. Krause, *Reregulation Or Clarification*, Traffic World, Sept. 28, 1998, at 40.

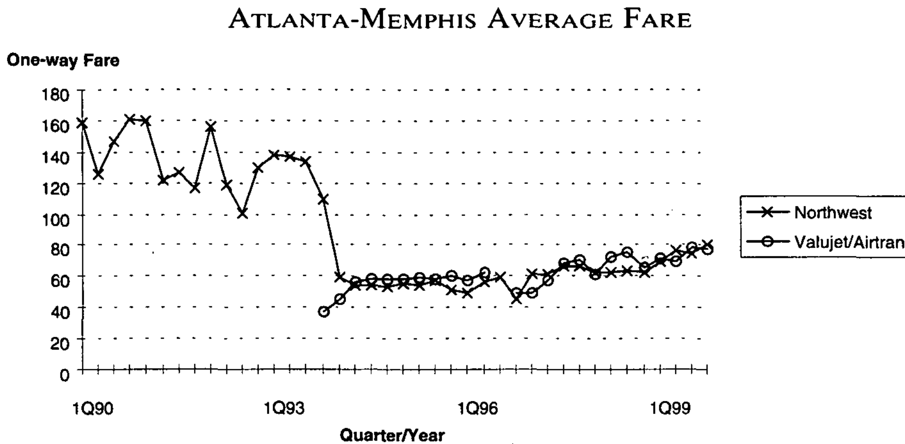
129. *See* Fred Allvine & John Lindsley, Increasing Monopolization of the United States Commercial Airline Industry Through the Development and Defense of Fortress Hubs 7 (1997).

130. Transp. Research Board, Entry and Competition in the U.S. Airline Industry: Issues and Opportunities C-2 (1999).

131. *Spirit Accuses Northwest of Predatory Pricing*, Airline Fin. News, Apr. 3, 2000.

132. Scott Thurston, *AirTran, Northwest In Feud Over Service to Minneapolis*, Atlanta Constitution, Apr. 5, 2000, at 17E.

ATLANTA-MEMPHIS AVERAGE FARE



Source: US Department of Transportation; Passenger Origin-Destination Survey.

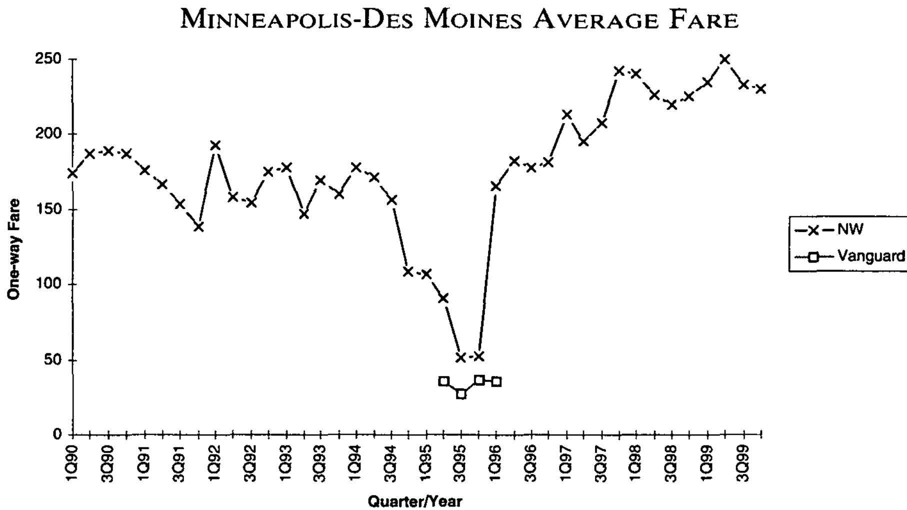
H. NORTHWEST VS. VANGUARD AIRLINES

Vanguard also complained to DOT about the anticompetitive practices of Northwest Airlines.[133] As the following chart reveals, Northwest Airlines responded sharply and swiftly to Vanguard's entry into the Minneapolis-Des Moines market, slashing air fares 68% in the third quarter of 1995 compared to average fares a year earlier. After Vanguard withdrew from the market, Northwest relentlessly raised fares to levels higher than ever have prevailed in the market. By the second quarter, Northwest charged an average of $244, over 400% more than the $48 fare it charged during Vanguard's brief appearance in the market.

The Minneapolis-New York market also tells an interesting story. Until 1997, Northwest Airlines served only New York nonstop at the LaGuardia and Newark airports. That year, it inaugurated nonstop service between Minneapolis/St. Paul and New York Kennedy International Airport. Coincidentally, Vanguard Airlines had inaugurated service in that market as well. Though Northwest's average fares in the Minneapolis/St. Paul-LaGuardia and Minneapolis-Newark markets averaged between $266 and $355 in late 1997 and early 1998 (about the range at which they had hovered at for several years), Northwest's average fares in the Minneapolis/St.Paul-Kennedy market ranged between $108 and $146. Fares remained at that level until the low-cost/low-fare competitor had been driven out. After Vanguard exited, Northwest raised its average fare to

133. Tony Kennedy & Greg Gordon, *Government Investigating NWA's Fares*, STAR-TRIBUNE, Feb. 27, 1998, at 1D.

MINNEAPOLIS-DES MOINES AVERAGE FARE



Source: US Department of Transportation; Passenger Origin-Destination Survey.

$141, 31% higher than a year earlier. After Sun Country Airlines entered the Minneapolis/St.Paul-New York Kennedy market, Northwest's offered average fares lower than Sun Country's. Since Northwest Airlines offers a first class product, and first class fares are included in DOT's average fare data, Northwest's coach fares were undercutting Sun Country's by a wider margin than suggested by the following chart.

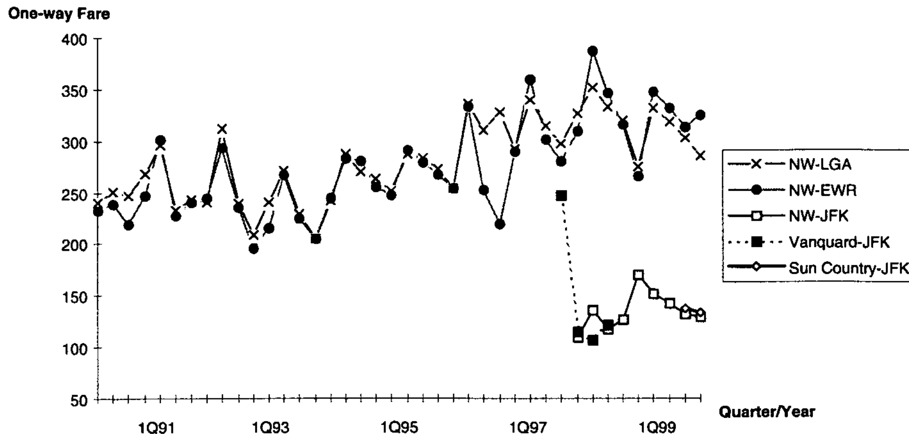
VII. NORTHWEST VS. SUN COUNTRY AIRLINES

A. SUN COUNTRY AIRLINES BEGINS SCHEDULED SERVICE AT MINNEAPOLIS/ST.PAUL

Inaugurated as a charter airline in 1983, Sun Country Airlines entered the scheduled airline business in the Minneapolis/St. Paul market on June 1, 1999. Until that time, Northwest was the only scheduled jet carrier based there, having absorbed Republic Airlines in 1986.

Northwest is the fourth largest airline in the United States, offering service throughout the country and to many foreign destinations. Northwest has more than 50,000 full-time-equivalent employees. In 1999, Northwest operated more than 400 aircraft, earning more than $9 billion in revenue. Northwest operates a large, profitable hub at Minneapolis, the eleventh largest airport in the United States. It has long-term lease agreements for 55 of the 70 available gates at the main terminal. Twelve more gates are being built and Northwest is seeking to lease ten of the twelve. Northwest has monopoly power in most of its Minneapolis/St.

MINNEAPOLIS-NEW YORK AVERAGE FARE



Source: US Department of Transportation; Passenger Origin-Destination Survey.

Paul city pairs. Before Sun Country's entry, Northwest had no nonstop competition on 12 of its busiest routes.

- Los Angeles (three airports)
- San Francisco
- Washington, D.C. (three airports)
- Boston
- Orlando
- Detroit
- Seattle
- San Diego
- Miami
- Milwaukee
- Indianapolis
- New York (LaGuardia)[134]

In markets where Sun Country now competes, Northwest had the following market shares in the first quarter of 1999 (prior to the inauguration of Sun Country's scheduled service):

Even in the short time since Sun Country began scheduled service, the extent to which the Minneapolis/St. Paul market has been constrained can clearly be seen. Traffic on many of the routes where Sun Country now competes had been stagnant for years, primarily attributable to Northwest's high fares. Following Sun Country's introduction of scheduled flights, traffic has jumped significantly. In fact, in the fourth quarter of 1999, traffic volumes were up 50% versus the same period a year ear-

134. MINNESOTA PLANNING, supra note 15.

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NORTHWEST AIRLINES' MARKET SHARE – MINNEAPOLIS/ST. PAUL CITY PAIRS 1ST QUARTER 1999		
City	NW Share %	Next Largest Carrier Share %
New York		
LaGuardia	88%	AA - 2%
Kennedy	49%	TW - 44%
Boston	85%	AA - 4%
Washington, DC		
Dulles	84%	UA - 11%
Reagan National	88%	UA - 5%
San Francisco	82%	UA - 9%
Los Angeles	79%	UA - 6%
Seattle	82%	UA - 8%
Detroit	97%	AA - 1%
Milwaukee	99%	UA - 1%

Source: US Department of Transportation; Passenger Origin-Destination Survey.

lier. Also recognize that the growth has not come at the expense of Northwest, a clear indication that there is room for both carriers to operate profitably in the Minneapolis/St. Paul market.

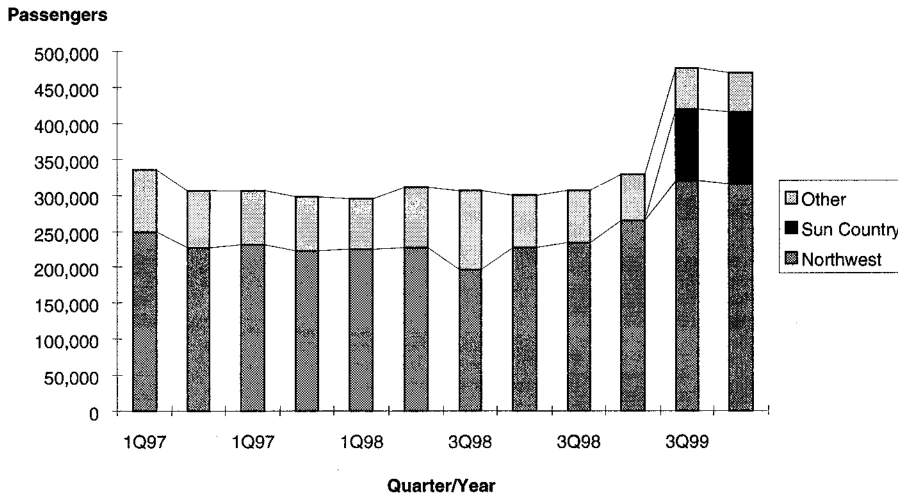
As described above, the record of the last decade reveals that Northwest repeatedly responds aggressively to new entry so as to protect and expand its monopoly power. Any time that a low fare carrier attempted to enter Northwest's monopoly markets, Northwest engaged in a predatory response designed to drive the low fare choice from the market, and to serve as a painful example to any other potential competitor. More specifically, Northwest's repeated practice of dumping large quantities of low fare seats into a specific market, coupled with its frequent flyer program and schedule frequency advantages, inflicts unacceptable economic pain on the low fare competitor which has resulted in the competitor leaving the market. Following its departure, the benefits to consumers and businesses of a low fare choice are soon gone as Northwest again raises fares to monopoly levels.

Though Northwest exhibited a relatively benign competitive response when faced with Sun Country's presence in Minneapolis/St. Paul as a charter airline, it would adopt a significantly different approach to that carrier as a scheduled airline, one expanding beyond the types of predatory conduct described above.

B. NORTHWEST DROPS FARES SHARPLY

Northwest's response to Sun Country's foray into the scheduled mar-

TOTAL MSP MARKET SIZE—BY QUARTER COMPETING SUN COUNTRY/NORTHWEST ROUTES



Source: U.S. Department of Transportation; Minneapolis/St. Paul Origin and Destination Traffic

ket was to radically lower its fares in city-pair markets in which Sun Country entered, while increasing flight frequency and seat capacity.[135] Across the board, in every market Sun Country entered, Northwest dropped its 7-day advance purchase fares by an average of 45-67% in April 1999, following Sun Country's announcement of scheduled service earlier that year.

Northwest claims that its response to Sun Country in the Minneapolis/St. Paul-Los Angeles market was only on advance-purchase fares, and had more restrictions than Sun Country's, imposing round-trip and Saturday night stay requirements. Northwest admits that it matched Sun Country's fares, but insists that occurred only on two flights a day.[136] Yet Northwest publishes fares that are at the same level as Sun Country in each market Sun Country entered. Northwest's fares carry a Saturday night stay restriction, except on flights in close proximity to those flown by Sun Country. The Saturday-night restriction is imposed to limit revenue dilution on business fares. Northwest describes Sun Country as an airline focused on the leisure travel market ("it continues to offer a service that on most routes is not well-structured for the business trav-

135. Letter from Minnesota Attorney General Mike Hatch to DOT Special Counsel Steve Okun (Apr. 23, 1999).
136. NORTHWEST REBUTTAL, *supra* note 5.

Transportation Law Journal, Vol. 29 [2001], Iss. 2, Art. 3

NORTHWEST AIRLINES' 7-DAY ADVANCE PURCHASE FARES FROM MINNEAPOLIS/ST. PAUL					
	Northwest July 1997	Northwest July 1998	Sun Country April 1999	Northwest April 1999	Northwest 1998 v. 1999
Detroit	$569	$602	$202	$202	-67%
Milwaukee	$294	$395	$202	$202	-49%
Seattle	$655	$582	$257	$257	-56%
San Francisco	$613	$501	$276	$276	-45%
Los Angeles	$630	$561	$276	$276	-51%
Phoenix	$489	$492	$239	$239	-51%
Las Vegas	$460	$870	$220	$220	-75%
Dulles	$590	$625	$257	$257	-59%
Orlando	$558	$501	$257	$257	-49%

eler.")[137] Thus, setting its restricted fares at levels well above Sun Country's enables Northwest to keep its business revenue high; Northwest's unrestricted fares set at Sun Country's levels are designed to keep Sun Country's load factor and revenue low.

Though Northwest was radically reducing fares in markets Sun Country had entered, it was keeping fares at extremely high levels where it faced no competition. The following table compares Northwest's lowest fares in Minneapolis/St. Paul markets Sun Country has entered, *vis-à-vis* Northwest's lowest fares in markets of comparable stage length in which there is no low-fare competitor:

Northwest's actions in the Minneapolis/St. Paul-Milwaukee market demonstrate why Northwest is widely regarded as the most aggressive airline in the industry. As reported to the DOT, by the fourth quarter of 1999, no more than six months after Sun Country started scheduled service, and no more than three months after Sun Country increased Minneapolis/St. Paul-Milwaukee service to twice-daily, Northwest was selling approximately 75% of its Minneapolis/St.Paul-Milwaukee seats at the lowest published rate, dropping its average one-way fare 59%, to $98 from the $234 average fare a year earlier.[138] According to the DOT, that was the fourth largest percentage decrease among all U.S. routes, and all U.S. carriers.[139] Northwest insists that Sun Country's two flights per day created enough capacity to capture all the local traffic in the market, and therefore Northwest's "revenue-maximizing response was to match Sun Country's fares more completely than it had done on other routes."[140]

137. *Id.*

138. Kennedy, *supra* note 69 at D-1. This data compares Northwest's average one-way fares in the Minneapolis-Milwaukee market during the fourth quarter of 1998 ($213) to the fourth quarter of 1999 ($98). In the fourth quarter of 1997, Northwest's average fares were $208.

139. *Id.*

140. NORTHWEST REBUTTAL, *supra* note 5 at 26.

NORTHWEST AIRLINES' LOWEST PUBLISHED MINNEAPOLIS/ST. PAUL FARES (SEPTEMBER 2000)		
City (asterisk denotes Sun Country market)	Lowest Published Fare	Stage Length (miles)
Seattle*	$130	1,395
Portland, OR	247	1.423
Spokane, WA	277	1,173
Boston*	$130	1,122
Hartford, CT	254	1,048
San Diego*	$130	1,531
San Jose, CA	304	1,573
Sacramento, CA	309	1,515
New York JFK*	$130	1,017
LaGuardia, NY	221	1,017
Newark, NJ	221	1,017
White Plains, NY	221	1,019
Philadelphia	204	978
Phoenix*	$130	1,276
Tucson, AZ	189	1,298
Las Vegas*	$ 99	1,300
Reno, NV	266	1,406

Of course, this wrongly assumes no stimulation of demand with low fares, by consumers who have avoided flying in the market because of Northwest's monopoly prices prevailing before competitive entry. Northwest also alleges that "Sun Country has an inexperienced management team, shifting and inconsistent business strategies, insufficient marketing infrastructure, and uncontrolled costs. If Sun Country fails, it has only itself to blame."[141] If Sun Country is so woefully inept, there appears to be no rational business explanation for Northwest's aggressive behavior in the Minneapolis/St.Paul-Milwaukee market, or any other. If Sun Country is incapable of running an airline successfully, why does not Northwest merely price at the revenue-maximizing level, and stand aside as Sun Country implodes?

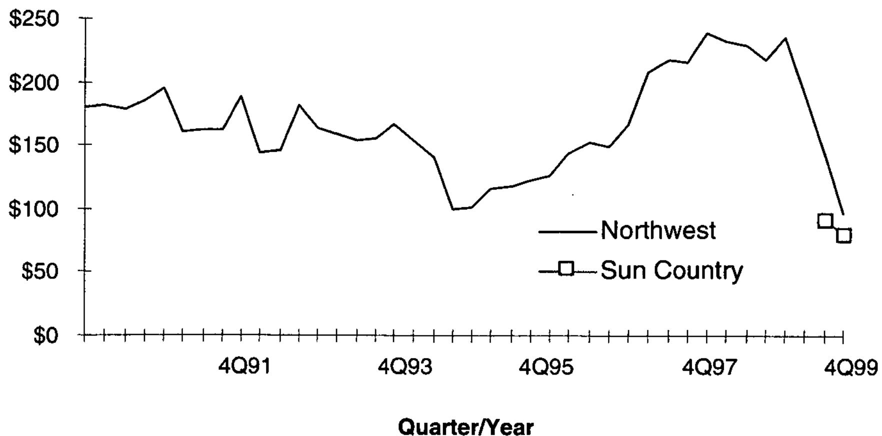
The U.S. Department of Transportation has observed:

> The network airlines . . . assert that an incumbent airline must respond with deep fare cuts and a large increase in the availability of discount seats to entry by a low-fare airline since the latter is allegedly capable of taking away all of the incumbent's local traffic. This assertion ignores the reality of the market. The claim that the existence of seats offered by a low-fare airline necessarily will cause the incumbent airline to lose a large share of its traffic is unconvincing. Incumbent airlines will keep much of their traffic due to their service features that are important to many travelers, especially busi-

141. *Id.* at 15.

Transportation Law Journal, Vol. 29 [2001], Iss. 2, Art. 3

MINNEAPOLIS/ST. PAUL—MILWAUKEE AVERAGE FARE



Source: US Department of Transportation; Passenger Origin-Destination Survey.

> ness passengers, such as attractive frequent flyer programs and more frequent flights, and their reputation for good service. In addition, the corporate fare discount programs offered by dominant airlines typically require a large share of the corporate customer's travelers to use that airline in order to qualify for the discounts, with the result that such corporate travelers will be unlikely to use the services of a new entrant. Experience demonstrates that a network airline can attract a substantial number of passengers, especially business travelers, even if a low-fare airline offers lower fares.[142]

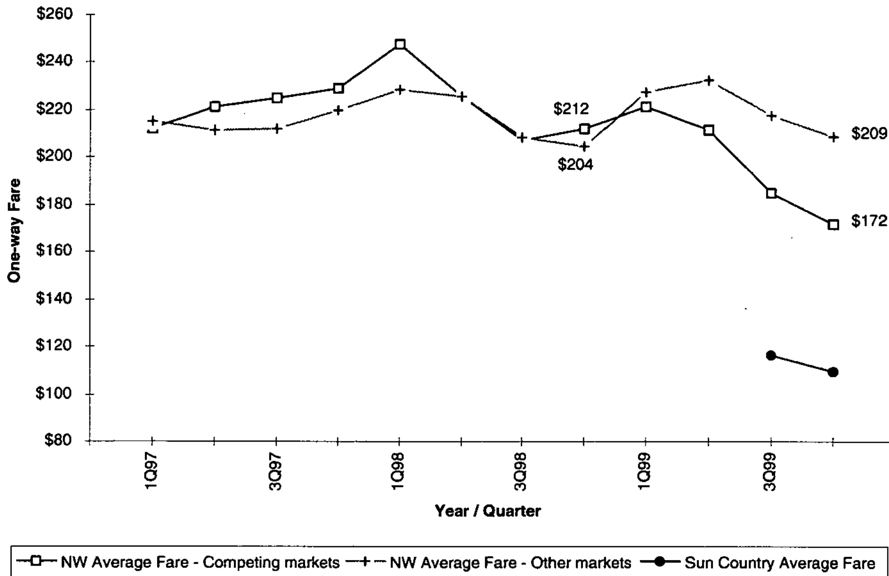
On average, by the fourth quarter of 1999, Northwest's one-way fare in competing Sun Country markets had fallen from $212 a year earlier to $172, nearly a 20% drop, while fares in all other Minneapolis/St.Paul markets had increased from $204 to $209 one-way. When criticized by Minnesota Attorney General Mike Hatch that it dramatically lowered fares when Sun Country entered its markets, Northwest insisted "these fare actions by Northwest are incremental adjustments to fare levels that have already been in these markets for an extended period of time."[143] Dramatic, certainly; incremental, not.

Finally, the way in which an incumbent carrier can subvert the ability of a new entrant to achieve break-even load factors is not only to drop prices to those offered by the new entrant, but to expand the number of

142. U.S. DEP'T OF TRANSPORTATION, supra note 10.

143. Response of Northwest Airlines to Letter of Minnesota Attorney General (May 28, 1999).

NW AVERAGE ONE-WAY FARE: SUN COUNTRY AND NON-SUN COUNTRY MARKETS



Source: US Department of Transportation; Passenger Origin-Destination Survey

seats offered at its lowest fare categories. In industry jargon, this is referred to as opening the low-fare "buckets". If the incumbent offers more additional low-fare seats than the new entrant, it can sop up discretionary demand like a sponge to water, particularly where it has stronger, established market identity, serves more cities with more flights, and offers a rebate in the form of frequent flyer miles. The following chart reveals the quantity of low-fare seats Northwest sold relative to Sun Country.

In its response to the Minnesota Attorney General's request for a DOT investigation of Northwest's competitive practices against Sun Country, Northwest alleged:

> Northwest's decision as to the extent to which it should match Sun Country's fares in each of these markets is the product of an assessment of what the profit-maximizing competitive response would be among various options under present market conditions. Northwest makes that assessment on the assumption that Sun Country would remain in the market forever—in other words, the determination of what is the profit-maximizing option does not rest upon the assumption that a particular option would drive Sun Country from the market . . . .[144]

144. *Id.*

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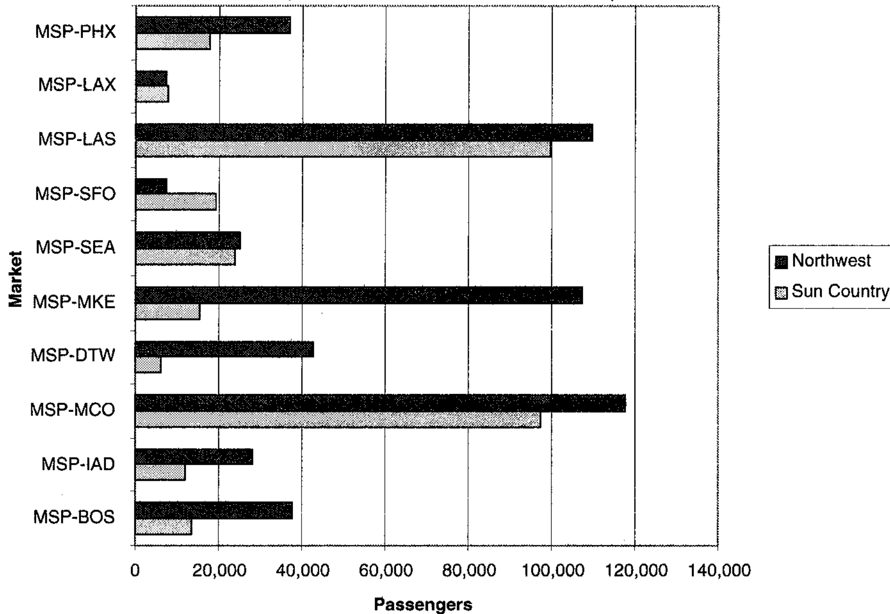
NORTHWEST V. SUN COUNTRY INCREMENTAL LOW-FARE SEATS SOLD TO & FROM MINNEAPOLIS/ST. PAUL (4Q99:2Q00 v. 4Q98:2Q99)



It is difficult to see how Northwest's 60% drop in average fare on its seven daily Minneapolis/St. Paul-Milwaukee flights is a profit maximizing response, in the short term, to a carrier that offers only two flights per day. And it's difficult to see how the addition of nearly 40,000 incremental low fare seats in the Minneapolis/St.Paul-Boston market is a profit maximizing response, in the short term, to a carrier that offers one flight per day, and sold an incremental 15,000 seats in that same market. As explained below, it is precisely such predatory behavior that the U.S. Department of Transportation has condemned.

C. NORTHWEST EXPANDS CAPACITY

Beyond these subversive pricing practices, Northwest also began to target markets that Sun Country entered with additional flights and seats. Northwest's capacity increases were larger in markets Sun Country entered relative to: (1) the overall growth of Northwest's system-wide capacity, (2) Northwest's historic rate of growth on these routes, and (3) Northwest's growth in the same markets from its Detroit hub. Moreover, Northwest's increased capacity in markets Sun Country entered despite the fact that these markets were experiencing declining operating mar-

gins, well below Northwest's average, as Northwest dropped its prices and expanded the number of low-fare seats offered.

The following is a representative sample of Northwest's capacity increases in markets Sun Country entered:

- *Minneapolis/St. Paul-Anchorage*—Northwest nearly doubled seats to (from 570 seats weekly in August 1998, to 950 seats in August 1999).
- *Minneapolis/St. Paul-Los Angeles*—Northwest changed its flight to match Sun Country's at the same departure time, and added wide-body 747 and DC-10 aircraft. Northwest's discount tour subsidiary, MLT, also added a twice-weekly DC-10 in the market.
- *Minneapolis/St. Paul-New York Kennedy*—Northwest inaugurated daily nonstops in May 2000.
- *Minneapolis/St. Paul-Orlando*—Northwest added a 6:00 a.m. aircraft in proximity to Sun Country's 6:45 a.m. flight.[145]
- *Minneapolis/St. Paul-Phoenix*—Northwest raised its capacity from five aircraft and 715 seats daily in June 1998, to six aircraft and 920 seats weekly one year later.
- *Minneapolis/St. Paul-San Antonio*—Northwest inaugurated twice daily nonstop service in June 2000, a market in which it theretofore had no service.[146]
- *Minneapolis/St. Paul-Seattle* - Northwest added an additional frequency.
- *Minneapolis/St. Paul-San Francisco* - Northwest added an additional flight and substituted a larger aircraft with more capacity to an existing flight.
- *Minneapolis/St. Paul-Boston* - Northwest added an additional flight.
- *Minneapolis/St. Paul-Houston* - Northwest added an additional flight.[147]

The following chart reveals Northwest capacity increases in Sun Country markets versus their capacity increases in all other non-stop markets from Minneapolis/St. Paul.

When viewed historically, or relative to Northwest's growth in Detroit, the aggressive capacity increase is equally evident. As shown in the following chart, Northwest had little interest in adding seats in Sun Country markets over the past decade, growing by less than 2% per year prior to Sun Country's entry. The same is true in Detroit where Northwest had negligible seat growth since 1990. Northwest's capacity decisions changed after Sun Country began scheduled service.

For a small carrier, offering one flight per day, Northwest's seat dumping dramatically reduces the potential for viable competitive service. Northwest's response to assertions by Minnesota Attorney General Mike Hatch that it dramatically increased capacity when Sun Country en-

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145. Letter from Minnesota Attorney General Mike Hatch to DOT Special Counsel Steve Okun (Apr. 23, 1999).

146. Testimony of Bill LaMacchia, Jr., Before the U.S. Senate Judiciary Comm., Subcomm. on Antitrust (May 2, 2000).

147. NORTHWEST REBUTTAL, supra note 5 at 27-28.

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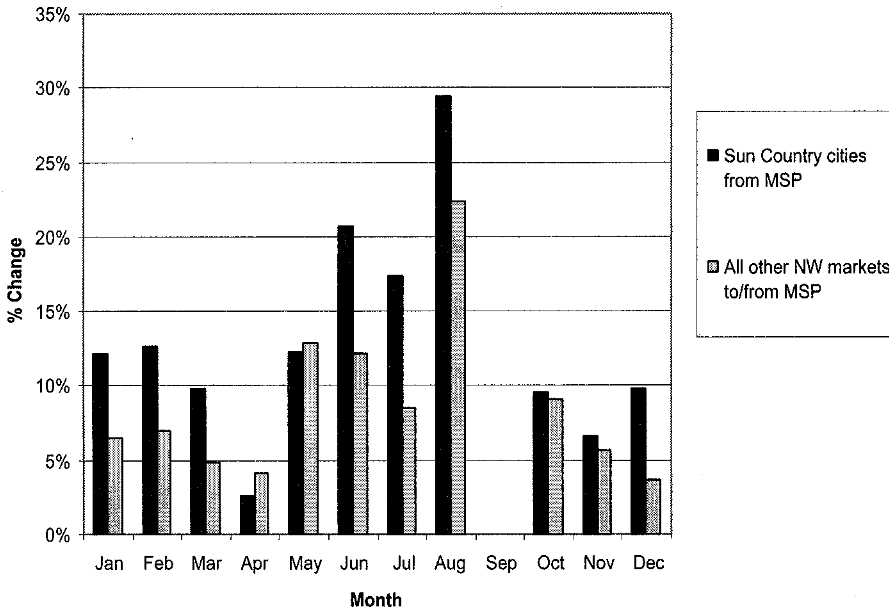
NORTHWEST & NORTHWEST AIRLINK CAPACITY INCREASES
99/00 v. 98/99



Source: US Department of Transportation; T-100 Monthly Operating Statistics by Carrier Entity January-April reflects 2000 v. 1999; April-December reflects 1999 v. 1998; September omitted due to labor strike in 1998

tered its markets was that "Northwest's decision to add capacity on some of the routes Sun Country is serving cannot possible be viewed as predatory. Indeed, those scheduling decisions were not a competitive response to Sun Country at all. Rather, they reflected decisions made by Northwest of where best to deploy a large number of additional aircraft available to Northwest this summer."[148]

One must ask why Northwest devoted additional frequencies and larger aircraft to markets in which it was dropping fares sharply, given the opportunity costs of not devoting that capacity to higher-revenue markets. Far from being a revenue-enhancing strategy, such circumstantial evidence suggests a different motive – to dump capacity in the markets Sun Country has entered in order to drive it from the market, sustaining short-term losses in order to re-exert its monopoly.

Northwest Capacity Growth Has Been Directed Toward Its Lowest Margin Routes

The above table demonstrates that Northwest's response to Sun

148. Response of Northwest Airlines, Inc., *supra* note 143.

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NORTHWEST SEAT GROWTH TO SUN COUNTRY CITIES FROM MINNEAPOLIS/ST. PAUL & DETROIT				
Destination	To/From Minneapolis/St. Paul		To/From Detroit	
	Before Sun Country Entered from MSP	After Sun Country Entered from MSP	Before Sun Country Entered from MSP	After Sun Country Entered from MSP
Boston	0%	5%	-2%	-1%
Detroit/Minneapolis	3%	0%	3%	0%
Washington (Dulles)	7%	22%	5%	-2%
Las Vegas	3%	13%	2%	8%
Los Angeles	-1%	12%	-1%	6%
Orlando	5%	23%	9%	-5%
Milwaukee	2%	3%	1%	3%
Phoenix	3%	9%	6%	4%
Seattle	1%	9%	5%	5%
San Francisco	1%	14%	-2%	-3%
Average	2%	9%	2%	1%

These data compare Northwest's growth rate in the pre-Sun Country period (4Q98, 1Q99, 2Q99 vs. 4Q90, 1Q91, 2Q91) with the post-Sun Country period (4Q99, 1Q00, 2Q00 vs. 4Q98, 1Q99, 2Q99). 3Q Omitted due to Northwest labor strike. Source: US Department of Transportation; T-100 Monthly Operating Statistics by Carrier Entity

Country has been to grow faster in markets served by Sun Country than it grew in non-Sun Country markets. This growth has been accompanied by massive price discounting and hence lower unit revenues and margins. This is the strategy of a predator - an airline intent on eliminating the low fare alternative. This is the strategy of a company seeking to regain its monopoly power. And it is surely not profit-maximizing behavior unless the profit sought is long-term profit extracted through higher fares from business and leisure travelers once the monopoly is re-established.

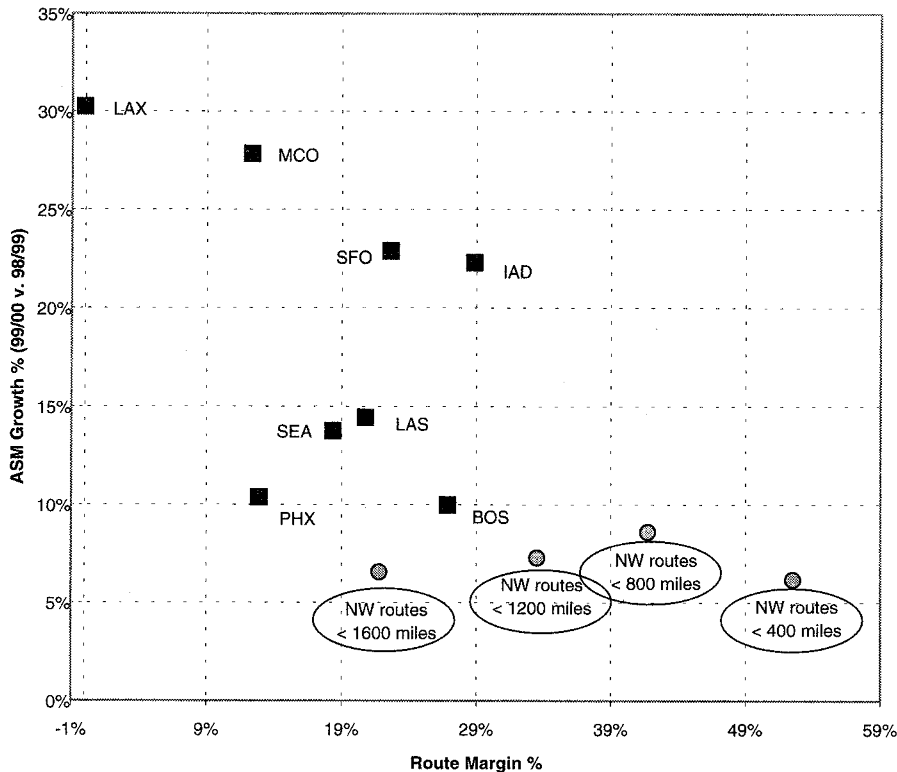
Northwest CEO John Dasburg defined predatory pricing as "deliberate pricing below profitable levels to undercut competition to the point that few airlines will survive."[149] By the standard of Dasburg's own definition, Northwest has crossed the line from competitor to predator.

D. NORTHWEST'S SUBSIDIARIES' RESPONSE TO SUN COUNTRY

Northwest also allegedly turned its partially-owned charter airline subsidiary, Champion Airlines, and wholly owned discount tour operator, MLT, against Sun Country after it became a scheduled airline. MLT and

149. David Phelps, *NWA Asks Pilots for a Giveback of $500 Million*, MINNEAPOLIS STAR TRIBUNE, July 15, 1992, at 1A.

NORTHWEST CAPACITY GROWTH V. ROUTE PROFITABILITY



Champion added flights and undercut fares on several of Sun Country's new routes, including the following:

- *Minneapolis/St. Paul – Las Vegas*—MLT increased to daily service on a route it had previously only flown twice per week each summer for the prior fifteen years.
- *Minneapolis/St. Paul – Los Angeles*—MLT offered round-trip charter fares of $239, undercutting Sun Country's lowest fare of $298.[150]
- *Detroit-Las Vegas*—MLT commenced twice-daily service after Sun Country expanded flights from four per week to daily. Northwest awarded its World Perks frequent flyer program miles to passengers who flew MLT out of Detroit, offered travel agent commission rates of 20%, agent cash bonuses of $10 per person booked, and published round-trip airfares as low as $99.90
- *Minneapolis/St. Paul-Orlando*—MLT went from twice-per-week service to daily service following Sun Country's scheduled entry into this market. MLT had operated its twice-weekly schedule since 1992.

Champion Air flew 32 weekly flights among seven routes Sun Coun-

150. Letter from Minnesota Attorney General Mike Hatch, *supra* note 145.

try inaugurated.[151] These pricing and capacity activities of tour operators and charter airlines are relatively unmonitored by the DOT, which collects data on scheduled airlines.

Sun Country is owned by Bill La Macchia, Sr., who also owns Mark Travel Corporation. It has been alleged that Champion and MLT have aggressively targeted Mark Travel Corporation since Sun Country inaugurated scheduled service at Minneapolis/St. Paul.

Minnesota Attorney General Mike Hatch asked the U.S. Department of Transportation to investigate Northwest's pricing and scheduling aimed at Sun Country. According to Hatch, "It is difficult not to conclude that the use of a three-front attack by NWA through Champion, MLT and its own carriers creates a climate of expanded seating, reduced prices and scheduling conflicts designed to push an emerging competitor out of this marketplace. . . . I believe NWA may be in engaging in activity prohibited by your guidelines."[152] Northwest, with revenues of $11 billion, an organization nine times the size of Mark Travel, owning 100% of MLT, responded to assertions that it used MLT as a competitive weapon against Sun Country by saying, "MLT draws no significant competitive strength from its affiliation with Northwest. In the charter tour operator business, Sun Country/Mark Travel is Goliath and MLT is David. In that world, MLT has no market power."[153]

E. Northwest Cancels Cooperative Agreements

In the fall of 1998, Northwest canceled agreements with Sun Country at Boston and Los Angeles to provide ground services and office and ticket counter space, preferring to leave such space vacant rather than leasing it to Sun Country.[154] In February 1999, Northwest Senior Vice President Richard Hirst assured the Minnesota Attorney General that, "Northwest has historically provided Sun Country Airlines with a wide range of services and facilities. . . . [I]t is not our policy and never has been our practice to use airport facilities and vendor services as competitive weapons."[155]

Yet soon thereafter, Northwest was doing precisely what Hirst had assured the Attorney General it would not do. Northwest canceled its maintenance and training agreement and certain airport rentals, refused

151. Eric Torbenson, *U.S. Probe of Northwest Airlines' Pricing, Schedules Sought*, St. Paul Pioneer Press, Apr. 29, 1999.

152. Torbenson, *supra* note 151; *see also* Tony Kennedy, *Hatch Asks Federal Officials To Watch Northwest's Response to Sun Country*, Minneapolis Star Tribune, Apr. 29, 1999, at D-3.

153. Response of Northwest Airlines, Inc., *supra* note 143.

154. Testimony of Bill LaMacchia, Jr., *supra* note 146.

155. Beth Hawkins, *Dirty Little Air War*, City Pages, November 3, 1999.

to sell or loan parts to Sun Country, and upped its hangar rent. Only days after Sun Country entered the scheduled market at Minneapolis on June 1, 1999, Northwest violated long-standing industry etiquette by refusing to continue its 16-year pact to share parts and testing equipment. Northwest sent out a company-wide memorandum ordering its employees to bar Sun Country from buying or borrowing spare parts: "effective immediately, all parts support (loans/sales) to Sun Country is terminated until further notice."[156] Because most airlines are committed to safety and customer service, the standard industry practice is to loan or sell other carriers parts on an "as needed" basis. No airline can maintain a full inventory of aircraft parts at all of the cities to which it flies. La Macchia observed, "If Northwest can disadvantage us and our customers are inconvenienced, they see that as a win for them."[157]

Northwest next closed its flight attendant and pilot emergency training facilities to Sun Country. According to Northwest spokeswoman Marta Laughlin, "if our decisions don't happen to please one particular airline - one that happens to be stealing our customers - then so be it."[158]

At the same time, Northwest chose to impede Sun Country's ability to compete by discriminating in travel agency commissions. According to Northwest, approximately 80% of its ticket sales are made by travel agents. While offering 5% commissions on most routes, it offers 8% commissions on routes flown by Sun Country. Northwest also offers "override commissions" to many of the largest travel agents in the state. These overrides are typically based on the share of traffic an agency tickets on Northwest relative to all other carriers. Given Northwest's extensive route network from MSP, many travel agents are unwilling to support a new entrant carrier and jeopardize these incentive payments from Northwest.

According to Sun Country Vice President Tammy Lee, "What Northwest is trying to do is to sew up every aspect of the community, dominate market share, and squeeze out competition."[159] Sun Country's Chairman, William E. La Macchia, concluded, "Rational businesses do not sell their products below costs, or pay travel agents bonuses to induce them to book passengers at drastically reduced rates or cut prices from 40%-60% except in hope and expectation that competition will be stifled and supracompetitive pricing will then compensate for losses."[160]

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156. *Id.*

157. Tony Kennedy, *NWA Stops Selling Sun Country Parts,* MINNEAPOLIS STAR TRIBUNE, Sept. 30, 1999, at D-1.

158. Eric Torbenson, *NWA Sun Country Conflict Heightens,* ST. PAUL PIONEER PRESS, Oct. 12, 1999, at C-1.

159. Hawkins, *supra* note 155.

160. Testimony of William E. La Macchia. Jr. *supra* note 146.

Sun Country Airlines was forced to cease scheduled operations from Minneapolis/St. Paul on December 9, 2001.

VIII. DOT POLICY ON UNFAIR EXCLUSIONARY PRACTICES

Between 1993 and 1999, the U.S. Department of Transportation received 32 informal complaints alleging unfair competitive practices. Half of these complaints involved complaints of unfair pricing and capacity responses to new entry – dumping low-fare capacity, and in some cases adding flights.[161] Since 1996, new entrants have tended to exit more routes than they entered. According to Professors Oster and Strong, "the slowdown in route entry may be due to the nature of responses by network carriers. . . . [T]he response of incumbents [to the entry of low-fare carrier Southwest Airlines] appeared to be very mild compared to the responses [of Northwest] to Reno Air and Spirit . . . ."[162] They observed that, "the decline in entry applications [after 1996], and in the number of carriers moving from authorized to operating status, may in part be due to the perceptions of both investors and prospective new entrants about the nature of likely entry responses from the incumbent carriers."[163] As Alfred Kahn has observed, "The entry of these new low-fare carriers keeps the industry honest . . . . I'm a strong advocate of competition and I don't want to go back to regulation. But you've got to distinguish legitimate competition from what is intended to drive competitors out and exploit consumers."[164] As Congress has observed, "Although the airline industry has been deregulated, this does not mean that there are no limits to competitive practices. As in the case with all industry, carriers must not engage in practices which would destroy the framework under which fair competition operates."[165]

John Nannes, Deputy Assistant Attorney General, US Department of Justice, speaking before the International Aviation Club, said:

> [I]n the 1980's the DOT approved a number of transactions involving carriers with high shares of city-pair traffic, reasoning that other carriers could easily enter those city pairs and discipline fares if the merging carriers began to act noncompetitively. Companies rarely engage in predatory conduct, it [was] said, because any attempt by the predator to 'recoup' the financial costs of predation in the form of higher prices after the prey is driven out will be defeated by new entrants undercutting those higher prices.

161. Oster, *supra* note 2.
162. *Id.*
163. *Id.*
164. Donna Rosato, *An Inside Look at DOT's Fight Against Airline Predation*, USA TODAY (April 6, 1998).
165. H.R. REP No. 98-793 (reporting on the CAB Sunset Act of 1984)

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> The airline industry exhibits certain characteristics that make a predation theory more than merely 'plausible'.
> First, hub carriers dominate hub markets, as demonstrated by market share. Second, hub carriers appear to be in a position to exact high fares, as demonstrated by hub premiums. Third, hub carriers can easily respond to entry by start-up carrier by increasing capacity and reducing fares in affected markets virtually overnight. ?Fourth, hub carriers have an incentive to act before start-up carriers develop a foothold in the hub: it is obviously easier to drive a carrier out before it gets established in the market. Fifth, a start-up is likely to have limited capital and is thus vulnerable to predatory practices; this is not an instance where anyone has to wait a long time to see whether competitors can be, or actually have been, driven out of business. Sixth, a hub carrier 'defending its turf' against encroachment by a start-up carrier in a few markets can create a 'reputation for predation' that deters start-up carriers from entering its many other hub markets; this can significantly alter the 'cost-benefit' predation calculation for a hub carrier in a way uncharacteristic of most other industries. In short, a 'recoupment scenario' is not implausible at all.[166]

The U.S. Department of Transportation became so concerned with the high failure rate of new entrant airlines, the widespread allegations of predatory pricing and capacity dumping, and the ineffectiveness of the antitrust laws to arrest it, that in 1998 it announced a proposed policy statement on unfair exclusionary practices.[167] The policy was designed to fill a void in the law which places the unfair competitive practices of virtually all U.S. industries, except airlines, under the jurisdiction of the Federal Trade Commission. Such jurisdiction instead resides with DOT.

As the Department of Transportation observed:

> A major carrier can minimize or even avoid self diversion of local revenue, for example, by matching the new entrant's low fares on a restricted basis (and without significantly increasing capacity) and relying on its own service advantages to retain high fare traffic. We have seen that major carriers can operate profitably in the same markets as low-fare carriers. Major carriers are competing with Southwest, the most successful low-fare carrier, on a broad scale and are nevertheless reporting record or near-record earnings.

166. John Nannes, Address Before the International Aviation Club (July 20, 1999).

167. Under the DOT's proposed guidelines, the DOT would initiate enforcement proceedings when one or more of the following occurs:
the major carrier adds capacity and sells such a large number of seats at very low fares that the ensuing self-diversion of revenue results in lower local revenue than would a reasonable alternative response,the number of local passengers that the major carrier carries at the new entrant's low fares (or at similar fares that are substantially below the major carrier's previous fares) exceeds the new entrant's total seat capacity, resulting, through self-diversion, in lower local revenue than would a reasonable alternative response, or the number of local passengers that the major carrier carries at the new entrant's low fares (or at similar fares that are substantially below the major carriers' previous fares) exceeds the number of low-fare passengers carried by the new entrant, resulting, through self diversion, in lower local revenue than would a reasonable alternative response. U.S. DEP'T OF TRANSPORTATION, *supra* note 10.

> Our enforcement policy will not guarantee new entrants success or even survival. Optimally, it will give them a level playing field.[168]

More recently, the Department of Transportation concluded:

> The most controversial competitive responses to entry have involved sharp fare cuts, a large increase in the number of seats sold at low fares, and often an increase in total capacity. . . .
>
> In some cases the incumbent network airline has . . . responded to entry in ways that appear to be economically irrational unless the entrant exits the market or reduces its service. In these cases the hubbing airline cuts its fares and increases the availability of its lowest fares by so much that it obtains much lower revenues and profits than it would have obtained if it had chosen a more moderate response. In extreme cases the incumbent airline cuts its fares to match the new entrant's fare levels, eliminates all or most of its restrictions on discount fares, and greatly expands the *availability* of discount-fare seats. The incumbent airline often adds flights as well. . . . [A]lthough the incumbent carries many more passengers, its total revenues are well below the revenues realizable through a more moderate response to entry.
>
> When the incumbent airline responds to entry by slashing fares and making low discount fares much more available, the new entrant airline usually cannot obtain enough traffic to sustain its service. The ready availability of low fares on the incumbent airline, which offers service features not offered by the new entrant airline and has an established reputation, dries up the traffic available to the entrant. The entrant must exit the market, and the incumbent airline then often increases its fares and sharply reduces the availability of its lowest discount fares.[169]

Northwest hired several economists to refute the allegation that predatory pricing exists in the airline industry, or that monopoly hub carriers exact a monopoly fare premium from passengers. Northwest CEO John Dasburg insisted, "Are we to believe today that the nation's air transportation system now depends upon the survival of a handful of thinly capitalized new-entrant airlines and, therefore, an interventionist policy is warranted and desirable?"[170] Northwest Vice President Elliot Seiden said, "What is really at work here is the sense that some firms are entitled to a break – let them get started, give them a shot, let them get their roots spread . . . . Our view is that's just a formula for slow death."[171] Competition is a formula for slow death? Is monopoly North-

168. *Id.*

169. U.S. DEP'T OF TRANSPORTATION, *supra* note 10.

170. *Dasburg Calls On Government to Halt Market Intervention*, AVIATION DAILY, Apr. 24, 1997, at 151

171. Lisa Zagarolli, *Why Feds Went After American*, DETROIT NEWS, July 20, 2000. Apparently, Northwest fears that consumers might prefer the services of low-cost/low-fare competitors to its own. Yet the antitrust and competition laws exist to allow consumers to choose among competitors, and not to allow the dominant firm to deny consumers of that choice.

west's formula for a long life?

Despite these well-funded efforts, the DOT concluded, "unfair competitive practices have occurred in the airline industry. Such practices are likely to cause consumers to pay higher fares and receive poorer service than they would obtain in a competitive market. The Department, working with the Justice Department, has an obligation to prevent such practices."[172]

IX. Northwest's Usual Response to Allegations That it is a Monopolist Which Engages in Predatory Conduct

As this Chapter has revealed, allegations of predatory behavior have been levied against Northwest Airlines on numerous occasions. Its response typically has been either to deny the substance of the allegations, attack the messenger, or alternatively, to admit the facts but offer a justification that it is merely competing fairly and lawfully. Northwest sometimes claims that there is no such thing as predatory pricing, though Northwest itself accused American of the same behavior.[173] Northwest also typically accuses its competitors of asking for a government bail-out, or of failing because of managerial ineptitude rather than anything Northwest has innocently done, though Northwest itself was bailed out by the State of Minnesota.[174] On occasion, Northwest claims that it is a large employer in Minnesota, and that its citizens should be grateful that Northwest has created a hub at Minneapolis/St. Paul. Frequently, Northwest will claim that fares appear higher at Minneapolis/St. Paul because the region has a higher proportion of business travelers, and because charter flights are capturing a portion of the low fare traffic. As noted above, Northwest has also alleged that its very existence potentially is threatened by low-cost/low-fare new entrant airlines.

But the allegations of predatory behavior are too numerous, and too oft-recurring, to be dismissed as random complaints of malcontent airlines seeking to blame others for their ills. Northwest's prices in the nonstop markets where it faces no competition (or faces only another high-cost/high-fare megacarrier) are too high to deny the existence of a monopoly, and consumer exploitation. And if Northwest insists that the exorbitant prices it charges in its monopoly markets are in fact *reasonable*, and that it operates in an industry with very thin margins, then most cer-

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172. U.S. Dep't of Transportation, *supra* note 10.

173. Northwest has claimed, "There is no evidence that major carriers are engaged in predatory pricing." Reply Comments of Northwest Airlines in DOT Docket OST-98-3713-1594 (Sept. 8, 1998).

174. Northwest has insisted that "There is no evidence that new entrant failure is the result of major carrier competitive responses." Reply Comments of Northwest Airlines in DOT Docket OST-98-3713-1594 (Sept. 8, 1998).

tainly the radical price discounts Northwest offers in response to a new entrant are below-cost, and therefore predatory.

Why does Northwest suffer massive opportunity costs in the form of taking aircraft out of monopoly markets, where they are producing supracompetitive profits, to re-deploy them into markets where seats are overwhelmingly discounted? Why does Northwest sharply drop prices and increase capacity in nonstop markets where low-fare new entrants appear, while consistently maintaining high prices in markets where they are absent? The answer is clear—Northwest is willing to suffer short-term losses in order to drive new low-fare competitors out of Minneapolis/St. Paul, out of Detroit, and out of Memphis, where it maintains monopoly hub operations.

Northwest has the financial ability to weather a predatory storm longer than a new entrant. Its message is clear – new entrant competition with Northwest is the equivalent of challenging a blood bank to a bleeding contest. Northwest has monopoly spokes radiating from each of its hubs that can cross-subsidize its losses in spokes in which low-cost/low-fare competition appears. The predatory battle is waged in order to raise prices sharply once the new entrant departs, and resume its monopolistic exploitation of consumers in all the spokes radiating from its Fortress Hub. If there is no such thing as unlawful predatory pricing, what did Northwest CEO John Dasburg mean when he said, "In the long run, predatory pricing will reduce the number of airlines, ultimately cutting the number of flights and choices available, particularly in smaller markets. This will leave the few surviving airlines free to price just as high as they want for just as long as they want. You will bear the cost of this"?[175] Is pricing predatory only when it is directed *against* Northwest?

Several Fortune 1000 companies are headquartered in Minneapolis/St. Paul, Detroit, and Memphis. But 3M Company does not charge Minnesota consumers more for Scotch Tape than it charges out-of-state consumers; Ford Motor Company does not charge more for Ford Explorers in Michigan than it charges elsewhere; FedEx does not charge more to ship packages from Memphis than it does from another city. The fact that Northwest Airlines is a major employer in Minnesota gives it no license to exploit consumers and use its predatory muscle to suppress competition designed to provide a modicum of consumer relief.

Northwest's large employee base has afforded it considerable political power to suppress efforts to build a new airport at Minneapolis/St. Paul, to persuade airport authorities at its hubs to favor it over new entrants, and to persuade Minnesota politicians to deliver up several hun-

175. David Phelps, *NWA Asks Pilots for a Giveback of $500 Million*, MINNEAPOLIS STAR TRIBUNE, July 15, 1992, at 1A.

dred millions of dollars in taxpayer guaranteed debt financing. To claim, as Northwest does, that small airlines which seek government relief from monopolistic, predatory, and exclusionary practices is the equivalent of asking for a government bail-out, is both to misunderstand that a bail-out is an economic subsidy, and to engage in unashamed hypocrisy.[176] The competition laws apply to all monopolists; airlines are not exempt. To ask for their enforcement is merely to ensure that competition disciplines pricing and service as it does in every other American industry.

Northwest's assertion that the "hub premium" is instead a reflection of a higher mix of business travelers does not seem to acknowledge that high fares lead to less travel by all but the most price-insensitive. Beyond that, it is unclear why major airlines, such as Northwest, believe that businesses must necessarily continue to pay high prices. And although Northwest will claim that fare data in the Minneapolis market is skewed by not recognizing charter activity, it has again confused the symptom with the cause. The presence of charter activity is an indication of high scheduled fares in a dominated market.

Finally, the allegation that competition might cause the "slow death"[177] of Northwest is a startling admission of a lack of self-confidence by management of one of the world's largest airlines, one which dominates three major American hubs, and flies to several Continents. In fact, several smaller metropolitan areas (including Denver, Salt Lake City, and Phoenix) have an established low-cost/low-fare competitor, and the dominant airlines (United, Delta, and America West, respectively) do not make this claim that somehow competition will destroy the world as we know it. At airports where competition exists, taking advantage of the price elasticities of demand inherent in air travel, the low-cost/low-fare carrier stimulates the market with discretionary traffic growth. According to the U.S. Department of Transportation, "Virtually all domestic traffic growth in recent years is attributable to the spread of low cost service. . . . [T]o a great extent low fare service attracts new passengers to the industry rather than simply diverting traffic."[178] The incumbent and new entrant airlines *both* enjoy higher load factors, filling seats which otherwise would fly empty. Far from destroying the incumbent, competition encourages it to provide better service to consumers, making it a

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176. It was Northwest that sought and received a State of Minnesota government bail-out. It was Northwest that sought Federal court protection from the actions of a larger competitor when it felt threatened. It was Northwest that threatened bankruptcy to obtain employee wage concessions. It is Northwest that has sought anti-trust exemption so that it could form cartels with other large airlines. It is Northwest that places a high value on its Tokyo hub because it is severely constrained by government controlled slots. And it is Northwest that has a political action committee and a Washington office dedicated to lobbying.

177. Zagarolli, *supra* note 171.

178. U.S. DEP'T OF TRANSPORTATION, THE LOW-COST SERVICE REVOLUTION 2, 16 (1995).

stronger and more sustainable enterprise. Monopolies tend to be high-cost, high-priced, low-service enterprises. Competition can breathe new life into such a lethargic corporate culture, causing it to reduce its costs, lower its price, and improve its service. In a service industry such as commercial aviation, such competitive discipline is essential to long-term sustainability.

One must recall the impact of the flood of Japanese automobiles into the U.S. market in the 1960s and 1970s. Far from destroying the U.S. auto industry, it inspired General Motors, Ford and Chrysler to new levels of productivity, efficiency, and quality. And by giving consumers more dependable, durable, and reliable automobiles, it enabled Detroit automakers to enjoy record profitability.

Sometimes Northwest alleges that those who urge enforcement of the competition laws are trying to re-regulate the airline industry.[179] When one hears such a claim, one must remember the words of the father of free market capitalism, Adam Smith, who wrote:

> By a perpetual monopoly, all the other subjects of the state are taxed very absurdly in two different ways; first, by the high price of goods, which, in the case of free trade, they could buy much cheaper; and secondly, by their total exclusion from a branch of business, which it might be both convenient and profitable for many of them to carry on. It is for the most worthless of all purposes that they are taxed in this manner. It is merely to enable the company to support the negligence, profusion, and malversation of their own servants [managers and employees] whose disorderly conduct seldom allows the dividend of the company to exceed the ordinary rate of profits in trades which are altogether free, and very frequently makes it fall even a good deal short of that rate.[180]

Fair competition obviates the need for monopoly regulation.

X. Conclusion

> "There have been instances in which a new, small carrier has offered low price service between a major carrier's hub and a spoke city, only to find the major carrier cutting its own air fares and increasing the number of seats—or even airplanes—on that route and sacrificing short term profits with only one goal in mind: to drive the new entrant out of the market and then raise its own fares to their original level or higher, and cut back its service."
>
> The U.S. Department of Transportation[181]

One source described Northwest Airline's anticompetitive activities

179. Northwest Rebuttal, *supra* note 5.

180. Adam Smith, An Inquiry Into the Nature and Causes of the Wealth of Nations 712 (E.P. Dutton 1910).

181. U.S. Dep't of Transportation, *DOT Releases Airline Competition Policy Statement* (Press Release Apr. 6, 1998).

in these words: "Northwest's tactics – matching cut-rate fares, surrounding flights of smaller competitors and other attempts to exclude upstart carriers from some markets – show how established airlines use their economic power and tools such as bigger jets and fleets, travel agency bonuses and gate domination to protect their turf from fare-cutting challengers."[182]

Minneapolis/St. Paul travelers pay some of the highest air fares in the nation – up to 49% higher than the national average for trips of comparable distance. The monopolization of Minneapolis/St. Paul International Airport began with Northwest's acquisition of its largest competitor, Republic Airlines in 1986. That merger gave Northwest the means to raise prices sharply. In 1989, a leveraged buy-out of Northwest Airlines saddled its balance sheet with more than $3 billion in debt. Minneapolis/St. Paul passengers and Minnesota taxpayers have, in effect, been asked to pay down that debt through higher fares and government subsidies. The net drain on the Minnesota economy is several hundreds of millions of dollars per year.

Monopolistic pricing is possible only if competition is suppressed. Among all major U.S. airlines, Northwest has been the most aggressive in attacking any low-cost/low-fare airline which attempted to enter its fortress hub. Over the past decade, several low-cost/low-fare carriers have been attacked by Northwest, including Reno Air, Spirit Airlines, Pro Air, Western Pacific, Kiwi International, Access Air, AirTran, and Vanguard Airlines. The response in every case was to use predatory pricing to deny the new entrant break-even load factors by flooding the market with sharply discounted seats. Once the injured competitor withdrew, Northwest reinstated prices to their monopolistic levels.

In 1999, a Minneapolis/St. Paul-based charter airline – Sun Country Airlines – transformed itself into a scheduled airline. The response by Northwest was to aggressively attack Sun Country with additional flights and larger aircraft, coupled with an avalanche of discount seats in every market in which Sun Country attempted to compete. Northwest canceled agreements with Sun Country for leased space, training, and parts. Northwest's charter and tour operator subsidiaries added flights and undercut fares in markets Sun Country had entered. The nation's most aggressive major airline became even more aggressive in attempting to deny Minnesota travelers a competitive choice. On December 9, 2001, Sun Country was forced to terminate its scheduled operations.

Northwest's success in driving another competitor from Minneapolis/St. Paul may encourage it to do what it has always done – raise prices sharply to their previous monopolistic levels. As Northwest reestablishes

182. Zagaroli, *supra* note 171.

its monopoly, it will be highly unlikely that another new entrant airline will dare try to take on Northwest from its Minneapolis base. Ironically, the people who will pay the price of monopolization are the citizens who came to Northwest's rescue with a bail-out, and the taxpayers who built, and own, the very airport that Northwest seeks to monopolize.

If major hub-dominant airlines are free to price below cost and increase capacity or flight frequency significantly, a new entrant will find consumer demand for its product eroded below a break-even cost level. Though the incumbent will lose money in the short-term, it will recoup those losses in the long-term.

The competitive response of a major airline to the entry of another major airline into its hub is generally not to dump capacity or price below-cost, for such a predatory effort would be futile. But when a less-well-capitalized, younger, low-cost new entrant airline attempts to enter, the competitive response is often predatory, with the intent of driving the new entrant out of the market. Chronologically, the process is this:

1.) Major airline establishes dominance at airport serving major city.
2.) Dominance allows major airline to price well above competitive levels.
3.) When a new entrant attempts to enter a major airline's hub, dominant airline responds with below-cost pricing, capacity dumping, and/or a number of other predatory practices until the new entrant is driven out.
4.) Once the new entrant is driven out of the market, dominant airline raises prices to levels sometimes higher than those prevailing before the new entrant attempted entry.

Predatory behavior can have a chilling effect on new entry. As Irwin Steltzer observed, a hunter who walks past a field with a no trespassing sign may ignore it, unless the field is littered with bodies of previous trespassers. Similarly, Mark Atwood concludes, "Fear of predation shrinks the available pool of investment capital for upstart airlines and channels their entry away from the very (monopoly) markets where their competitive presence would be most valuable" to the consuming public, relegating them to the small, safe niches of the airline market.[183]

Reviewing this pattern, which has appeared again and again over the past two decades, Alfred Kahn concluded:

> When I am confronted with that objective sequence of events, I am prepared to characterize the response of the incumbents . . . as predatory, and I see no reason to require any further demonstration. I think the most grievous governmental failure in the recent years has been the failure to prosecute a single case against new competitors, and I certainly applaud the Department of Transportation for undertaking a vigorous enforcement effort. . . .

183. Mark Atwood, Refining Predatory Policy: The Fear Factor and Reduced Funding for Low-Fare Airlines, ANTITRUST LAW & ECON. REV. 89 (1999).

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The acid test, whether it is framed in terms of a predatory intent or in terms of the likely objective of anticompetitive consequences . . . is whether the incumbent airline is deliberately accepting financial losses selectively in the markets where it is subject to competitive challenge, engaging in what Corwin Edwards 50 years ago called discriminatory sharp-shooting. For the reasons that the DOT clearly expands, a policy of deliberately losing money would not make sense except on the expectation of driving people out and being able to recover it. . . . The scores of competitors that have entered the industry over the last 20 years attest to the widespread eagerness of enterprisers to take the risk of coming in and competing in free markets. But the history of their entry and demise also demonstrates that we must have vigorous antitrust-like policies to keep open the opportunity for that entry, free of the threat, apparently abundantly demonstrated by actual practice, of predatory responses.[184]

If Neiman-Marcus, Saks, Sears and Montgomery Wards had lowered their prices to Wal-Mart's levels, while building stores several times their size right across the street of every newly opened Wal-Mart, consumers would have been denied the opportunity to buy consumer goods at discount prices. It is consumer choice that our competition laws must protect. This is particularly true in industries which market their wares from publicly-owned, taxpayer-financed facilities, like airports.

To survive, low-fare competitors need reasonable access to airport facilities, the cessation of predatory conduct, and the support of the flying public. Supporting competition and identifying the predatory actions of any monopoly is not just the responsibility of government regulators, it is also the responsibility of business leaders and consumers. Competition is good for consumers, good for businesses, and good for the regional economy which relies on high quality, reasonably priced air transportation.

Northwest Airlines has become the most aggressive major airline in protecting its monopoly status. There is another way. There are several examples of where a major hub carrier and a low fare alternative both operate successfully in the same city: United and Frontier in Denver; Delta and AirTran in Atlanta; TWA (soon American Airlines) and Southwest in St. Louis; America West and Southwest in Phoenix; and Delta and Southwest in Salt Lake City. This is not a "zero sum game" where one airline gains at the expense of another—a low fare competitor enlarges the market, provides additional consumer choice and makes the larger competitor more responsive to the marketplace.

As the Department of Transportation identified:

Low fare carriers' success relies on having such low costs that they can offer prices that incumbent carriers cannot match for large proportions of their

184. Testimony of Alfred Kahn Before the U.S. Senate Comm. on Commerce, Science & Transportation (Apr. 23, 1998).

> capacity. What this means is that to a great extent low fare service attracts new passengers to the industry rather than simply diverting traffic from the network carriers. And network carriers still have advantages that enable them to compete at higher cost levels. They have an advantage in flow traffic, which allows them to shift capacity from local passengers to flow passengers in order to maintain adequate revenues, and they typically have advantages in frequent flyer programs and travel agent commission overrides. Thus, while network carriers probably can never match the lower unit costs of point-to-point operators, they do not have to. Rather, they have to narrow cost differences to the point that their competitive advantages on the revenue side provide a competitive equilibrium.[185]

There are several reasons why Northwest should cease its predatory behavior:

- First, a low fare competitor does not threaten the viability of Northwest. To the contrary, a low fare competitor will expand the market place for all, including Northwest.
- Second, a hub competitor will improve Northwest's service quality by giving customers a choice.
- Third, allowing a low fare competitor a chance to compete will reduce the risk of antitrust enforcement litigation against Northwest.
- Fourth, the consumers traveling to and from MSP airport want and deserve a choice. Northwest will further damage its reputation by driving yet another low fare choice from the market place. Consumers and business travelers resent not being allowed a choice.

Undoubtedly, an airline like Northwest has a place in the market. It will continue to be the largest airline in several cities, despite the fear expressed by Northwest executives that allowing low-cost/low-fare competition will produce Northwest's "slow death." Through its vast network and enormous fleet, Northwest can provide more frequent service to an array of destinations around the world than can a smaller competitor. But price-sensitive consumers still deserve a choice. The effort of a monopolist to deny consumers that choice is illegitimate, if not illegal.

The monopolization of public resources is antithetical to the public interest. The purpose of airline deregulation was to promote competition, not allow airlines to monopolize public resources. Monopolies generally bring high prices and poor service quality. Predatory behavior by a monopolist to suppress competition should not be tolerated under U.S. competition law.

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185. U.S. DEP'T OF TRANSPORTATION, *supra* note 178.